



**FINAL REPORT**  
**MANAGEMENT REVIEW OF VERMONT'S**  
**NONPROFIT HOUSING DEVELOPMENT**  
**ORGANIZATIONS**

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## 1.0 Introduction

### Project Background and Study Objectives

The Vermont Housing and Conservation Board (VHCB) is a quasi-public, State-supported funding agency that provides grants, loans and technical assistance for the development of perpetually affordable housing and for land conservation. With respect to its housing activities, VHCB provides funds predominantly to nonprofit housing development organizations. These nonprofit housing organizations are private corporations with federal 501(c)(3) status and are geographically dispersed in housing markets across the State. A wide range of housing types are eligible for VHCB funding including rental housing, rental and ownership co-ops, mobile home parks, single family homes, shared elderly housing, single room occupancy housing, and group homes. VHCB funding, in the form of loans and grants, is available for housing acquisition, rehabilitation, and new construction. Since its creation in 1987, VHCB has supported the development of more than 7,000 units of affordable housing.

In December of 2003, the State of Vermont Agency of Administration in coordination with the Department of Housing and Community Affairs (DHCA) contracted with ICF Consulting to conduct a management review of nonprofit housing providers that have received multiple grant awards from VHCB. This review is one of a series of reviews that the State is currently undertaking to assess public service delivery mechanisms. As articulated by the Agency of Administration, the purpose of this study is to analyze both nonprofit developers' management of development projects and management of their organizations to determine the cost effectiveness and efficiencies of those management systems and to make specific recommendations to improve those systems while maintaining consistency with VHCB's enabling statute. The Agency of Administration formulated a comprehensive list of evaluation topics ranging from cost data on individual projects to the professionalism of organizations' development practices to a review of organizational financial statements.

### Project Scope

Of the fifteen nonprofit housing developers that regularly develop projects with VHCB funding, nine organizations were selected for inclusion in this study. These nine entities have developed approximately 75% of the units that have received VHCB support. These organizations, which are listed in the table below, were selected based on a desire to include organizations that represented the largest producers in terms of units while also including some smaller to mid-size producers. A total of 36 projects, four housing developments for each of the nine organizations, were selected for inclusion in the study, representing:

- The nonprofit's most recently completed project;
- A project completed by the nonprofit in either 1996, 1997, or 1998;
- The nonprofit's largest project (most units); and
- A "consultant's choice" project which the ICF team selected in consultation with Agency of Administration, DHCA, and VHCB staff.

Studied projects are listed in Figure One.

**Figure 1: Overview of Studied Projects**

Project Name/Town	Selection Criteria	# Units	New Construction / Rehab	Mixed Use?	Profile
<b>Brattleboro Area Community Land Trust (BACLT)</b>					
Western Avenue, Brattleboro	Most Recent	13	R	No	Rehab of three historic, formerly blighted properties in the Village center.
Westgate Apartments, Brattleboro	LP	98	R	No	Rehab of expired HUD 236 project, including infrastructure upgrades.
Laterre, Wilmington	CC	7	R	No	Rehab of dilapidated structure in village historic district
Germon's Mobile Home Park, Putney	1996-1998	22	MHP	No	Purchase of land and site improvements to mobile home park facing possible conversion/sale.
<b>Burlington Community Land Trust (BCLT)</b>					
Maple Tree Place, Williston	LP	50	NC	No	New construction, mixed income family rental units
Bus Barns, Burlington	Most Recent	25	R& NC	Yes	Redeveloped idle industrial site into apartments, retail, and community space.
Park Place, Burlington	CC	34	R	Yes	Renovation of burned out historic structure in central business district.
600 Dalton Drive, Colchester	1996-1998	11	R	No	Historic renovation of eyesore property to provide units for HIV positive persons.
<b>Cathedral Square Corporation (CSC)</b>					
3 Cathedral Square, Burlington	Most Recent	28	R	No	Affordable assisted living project. Renovation of 21 elderly apartments and construction of 7 new units.
Ruggles House, Burlington	CC	15	R	No	Rehabilitation of historic structure to preserve affordable units for frail elders, including accessibility upgrades
McAuley Square, Burlington	1996-1998	74	NC	No	Intergenerational housing including senior enriched service units, and units for single parents
Heineberg, Burlington	LP	82	NC	No	81 units of enriched senior housing built on land donated by local seniors organization.
<b>Gilman Housing Trust (GHT)</b>					
Daniels Block, St. Johnsbury	Most Recent	25	NC	Yes	Reconstruction on burned out structure in central business district.

Project Name/Town	Selection Criteria	# Units	New Construction / Rehab	Mixed Use?	Profile
Moose River, St. Johnsbury	CC	28	R	No	Acquisition and renovation of blighted property, former federal Section 23.
Lind, Ryegate	1996-1998	7	R	No	Acquisition and gut rehab of seven historic row homes in village center, five year lease-purchase.
Shattuck Hill Mobile Home Park, Derby	LP	48	MHP	No	Acquisition of mobile home park including infrastructure upgrades and home replacements.
<b>Housing Vermont (HV)</b>					
Howard Block, Rockingham	Most Recent	13	R	Yes	Gut rehabilitation and reconfiguration of two fire-damaged downtown buildings, with first floor commercial space.
Exner Block, Rockingham	CC	10	R	Yes	Rehab of dilapidated and vacant historic downtown structure.
Holy Cross, Colchester	1996-1998	40	NC	No	New construction of senior units on land leased for \$1 from Catholic Church.
Northgate Apartments, Burlington	LP	336	R	No	Preservation of large subsidized property facing prepayment and market conversion/displacement of residents.
<b>Lake Champlain Housing Development Corporation (LCHDC)</b>					
O'Dell Apartments, South Burlington	LP	160	NC	No	"Turnkey" development of a large, mixed-income rental project.
Butler Block, St. Albans	Most Recent	6	R	Yes	Renovation of condemned historic downtown structure. First floor commercial with 6 upper apartments.
Richmond Village, Richmond	1996-1998	16	NC	Yes	Infill construction of townhouse style family units with 'home office' space in village center.
Swanton School, Swanton	CC	16	R	Yes	Renovation of vacant school building into elderly downtown apartments with first floor community health center and other social service space.
<b>Lamoille Housing Partnership (LHP)</b>					
Jeffersonville, Cambridge	LP	32	NC	No	"Turnkey" development of 32 units of mixed-income intergenerational affordable units.
Copley House, Morristown	CC	22	R	No	Renovation of historic structure into Level III care home for adults with severe and persistent mental illness.
Portland & Main, Morristown	Most Recent	11	R	Yes	Rehabilitation of historic structure in center of village into 11 apartments above Post Office, enabling Post Office to remain downtown.

Project Name/Town	Selection Criteria	# Units	New Construction / Rehab	Mixed Use?	Profile
Brewster River, Cambridge	1996-1998	7	R	Yes	Mixed income rental with small commercial space in village center.
<b>Regional Affordable Housing Corporation (RAHC)</b>					
Arlington Village, Arlington	LP	29	R	Yes	Rehab of eight historic structures and construction of two new infill properties in the heart of the village. Intergenerational, mixed-income, and commercial.
South & Benmont, Bennington	Most Recent	21	R	No	Rehab of 4 scattered site historic structures.
Manchester Knoll, Manchester	CC	20	NC	No	Mixed income townhouse style units for rent in downtown.
Cora B Whitney, Bennington	1996-1998	22	R	No	Adaptive reuse of old school house into senior complex with supportive services.
<b>Rutland Community Land Trust (RCLT)</b>					
Columbian Avenue, Rutland	Most Recent	9	R	No	Adaptive reuse of City owned structures.
Rutland Scattered Site, Rutland	LP	31	R	No	Scattered site rehab of nine eyesore foreclosed upon properties.
Union & Barlow, Brandon	CC	12	R & NC	No	Rehab of one historic structure and new construction of two additional units adjacent to downtown.
Hopkins & Royce, Rutland	1996-1998	12	R	No	Scattered site rehab of three structures and new construction of two additional structures.
<b>Legend:</b> LP=Largest Project CC=Consultant's Choice R= Rehab NC= New Construction MHP=Mobile Home Park					

These 36 projects contain a total of 1,392 units (representing roughly one-fifth of the units funded by VHCB since its creation). The projects represent a broad mix of development scenarios including rehabilitation (26 projects ranging from substantial renovation of existing housing to adaptive reuse of schools and industrial buildings), mobile home parks (2 projects), new construction (8 projects), and mixed-use commercial-residential (11 projects). The projects also take place over a large period of time, with completion dates ranging from 1989 to early 2004. The largest project, which involved the preservation of an HUD-insured property, had 336 units and the smallest project had six units. The diverse range of project profiles includes the following: elderly assisted living facilities, shared housing and independent efficiency/one-bedroom units, mental health facilities, reconfigured and modernized 3-story homes reconfigured into apartments for families, and the substantial renovation of hundred-unit townhouse-style, family housing.

Despite the variation among the projects, several distinct Vermont characteristics were evident. In general, the projects are small, with a median size of 22 units. Almost all of the projects serve multiple missions. In addition to the primary affordable housing mission, projects may also involve historic preservation, downtown revitalization and/or energy conservation. More than half of the projects have a high degree of development difficulty that would preclude them from being considered in jurisdictions that have alternative development options (such as new subdivision development).

### Data Sources

In preparing this report, ICF collected an extensive range of primary data from a variety of sources including project files, financial statements, staff interviews, and organizational questionnaires. ICF complemented these sources with a review of existing reports and management analyses, the purchase of cost data from Means and HomeTech, and interviews with housing professionals working in Vermont and in nearby states. ICF began field work in December 2003, with a trip to VHCB's offices to collect development cost data from project files. In early January 2004, a series of questionnaires were mailed to each of the nine nonprofits. From January to March 2004, ICF conducted site visits, lasting 2-3 days, to each nonprofit. During these site visits ICF verified responses to questionnaires, interviewed key organizational staff, and conducted brief visits to most of the 36 studied projects to gain a general sense of design/construction quality and property conditions. In June of 2004, ICF sent a second series of questionnaires to the nine nonprofits, seeking clarification of organizational financial data previously submitted by the nonprofits and requesting additional operations data on the current status of the 36 studied projects. Wherever possible ICF sought to obtain objective comparison data to provide perspective on the studied projects. However, in some instances where no comparison data or benchmarks were available, we have relied on "professional opinion," meaning the consensus judgment of the three senior project team members, each of whom has over 20 years of affordable housing experience in communities across the nation.

### Report Overview

This report is divided into the following sections:

- ❑ **Nonprofit's Management of Project Development** examines the nonprofit's management of the 36 housing projects in the study's scope. Factors that are analyzed include project costs, the professionalism of project development practices, and the consistency of projects with the VHCB statute and Vermont's Consolidated Plan.
- ❑ **Nonprofit Management** discusses the management capacity of the nonprofits as organizations. In addition to an overview of general management systems and an analysis of financial statements, the section gives particular emphasis to property and asset management functions.
- ❑ **The Vermont Housing Delivery System** comments on the roles of the many players in the systems, with special emphasis on the unique role of Housing Vermont.

- ❑ **Summary of Major Findings and Recommendations** provides ICF's overall assessment of the nonprofit housing developers and recommends a series of actions for improvement.

### Project Team

This management review was conducted by ICF Consulting with significant contributions from two subcontractors. Phil Jones of ICF Consulting served as the Project Manager, with assistance from Andy Zehe, Deputy Manager. Subcontractors Bob Santucci of Urban Renovation Consultants, Inc., and Stuart Hershey of Urban Ventures contributed substantially to all aspects of the project from fieldwork through analysis and reporting. Kim Gugino of ICF assisted with data tabulation and analysis. The ICF project team thanks all nine nonprofit organizations for their cooperation in providing information and helping us understand Vermont's unique affordable housing system. The contents of this report are solely the views of the ICF project team and do not necessarily reflect the views or policies of the Agency for Administration, DHCA, or VHCB.

## **2.0 Nonprofit Management of Project Development**

This section analyzes the nonprofits' management of the housing development process. The section begins with a summary of the extent to which studied projects were consistent with the Consolidated Plan priorities and then comments on the professionalism of nonprofit development practices. The section concludes with a discussion of development costs, including an assessment of the reasonableness of total development costs and an examination of cost components.

### **2.1 Consistency with Consolidated Plan**

The Consolidated Plan lists thirteen priorities, which are listed in Figure Two on the following page. ICF was asked to evaluate projects for consistency with the following subset of these priorities: service to very low-income and lower-income Vermonters; impact on historic preservation and downtown revitalization; creation of net new units; correction of health and safety problems; providing housing opportunities to Vermonters with special needs. Through the use of the Project Questionnaires, ICF asked nonprofits to identify how their projects served these key Consolidated Plan priorities. ICF found that 24 out of the 36 projects impacted historic preservation and/or downtown revitalization efforts. All thirty-six of the projects serve very low income Vermonters. Thirty-two out of the 36 projects created a net number of new units<sup>1</sup>. At least 15 out of the 36 projects corrected lead, asbestos, or other health or safety problems. Thirteen out of the 36 projects provided housing opportunities to individuals with special needs. These special needs housing projects often involved significant social service components such as assisted living for the elderly or on-site mental health care.

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<sup>1</sup> Eight of the thirty-two projects that produced net new units were new construction projects, and two additional projects involved a mix of new construction and rehabilitation.

Vermont's Consolidated Plan is demanding. In some instances compliance with the plan can increase development costs, but also provide additional benefits. For example, developments are usually located downtown near services and transportation, desirable locational factors which increase the market value for land, but which also provide important benefits to low-income households. Figure 2 below summarizes the project's compliance with the full range of Consolidated Plan priorities.

**Figure 2: Compliance with Consolidated Plan Priorities**

Grantee Initials	Project Name	Income	Historic / Downtown Revitalization	Creation of new net units	Health & Safety	Special Needs	Mobile Home Park	Rehab	Mixed Income	Families	Leverage	Accessibility	Upper Stories	Home-ownership
BCLT	Park Place	✓	✓	✓	✓			✓		✓	✓	✓	✓	
BCLT	Maple Tree	✓		✓					✓	✓	✓	✓		
BCLT	Dalton	✓	✓	✓	✓	✓		✓	✓		✓			
BCLT	Bus Barns	✓	✓	✓	✓			✓	✓	✓	✓	✓		
LCHDC	Butler/Lake	✓	✓	✓	✓			✓		✓	✓	✓	✓	
LCHDC	Swanton	✓	✓	✓	✓			✓			✓			
LCHDC	O'Dell Marketplace	✓		✓						✓	✓			
LCHDC	Richmond	✓		✓					✓	✓	✓	✓		
BACLT	Westgate	✓						✓	✓	✓	✓	✓		
BACLT	West Village	✓	✓	✓	✓			✓	✓	✓	✓	✓		
BACLT	Locus Hill	✓					✓	✓	✓	✓	✓			✓
BACLT	Laterre	✓	✓	✓	✓			✓		✓	✓	✓		
LHP	Brewster River	✓	✓	✓	✓	✓		✓		✓	✓	✓	✓	
LHP	Portland & Main	✓	✓	✓	✓			✓			✓	✓	✓	
LHP	Copley House	✓	✓	✓		✓		✓			✓	✓		
LHP	Jeffersonville	✓		✓						✓	✓	✓		
RCCLT	Union & Barlow	✓	✓	✓	✓			✓		✓	✓	✓		
RCCLT	Rutland	✓	✓	✓	✓			✓	✓	✓	✓	✓		
RCCLT	Hopkins	✓	✓	✓	✓			✓		✓	✓	✓		
RCCLT	Columbian	✓	✓	✓	✓			✓		✓	✓			
HV	Howard	✓	✓	✓	✓			✓		✓	✓	✓		
HV	Holy Cross	✓		✓					✓		✓	✓		
HV	Exner	✓	✓	✓	✓			✓			✓	✓	✓	
HV	Northgate	✓						✓	✓	✓	✓	✓		
CSC	Cathedral	✓		✓		✓		✓	✓		✓	✓		
CSC	Ruggles	✓	✓	✓		✓		✓	✓		✓	✓		
CSC	McAuley	✓		✓		✓				✓	✓	✓		

Grantee Initials	Project Name	Income	Historic / Downtown Revitalization	Creation of new net units	Health & Safety	Special Needs	Mobile Home Park	Rehab	Mixed Income	Families	Leverage	Accessibility	Upper Stories	Home-ownership
CSC	Heineberg	✓		✓					✓		✓	✓		
RAHC	Cora B Whitney	✓	✓	✓		✓		✓	✓		✓	✓		
RAHC	Ben-South	✓	✓	✓	✓			✓		✓	✓	✓		
RAHC	Manchester Knoll	✓		✓					✓	✓	✓	✓		
RAHC	Arlington	✓	✓	✓	✓			✓	✓	✓	✓	✓		
GHT	Daniels Block	✓	✓	✓	✓			✓			✓	✓	✓	
GHT	Shattuck Hill	✓					✓	✓	✓		✓			✓
GHT	Moose River	✓			✓			✓	✓	✓		✓		
GHT	Lind	✓	✓		✓			✓		✓		✓		✓

Source: ICF Questionnaires and VHCB Funding Memos

### Income Targeting

As noted above, one of VHCB’s statutory/Consolidated Plan priorities is service to very low-income and lower-income Vermonters. While all 36 studied projects provided units that served these income bands, the Agency for Administration asked ICF to provide additional analysis about the incomes of households being served and their rent burden (the percentage of monthly income spent on rent and utilities). To assist with this analysis, VHFA and VHCB provided rent rolls for 14 of the 36 studied projects, and VHFA provided administrative data on projects jointly funded by VHFA/VHCB.<sup>2</sup> In addition, ICF obtained administrative data on HOME-funded rental projects from the U.S. Department of Housing & Urban Development (HUD), which allowed for comparisons of income targeting across different states.

The 14 projects for which VHFA/VHCB provided rent rolls totaled 322 *occupied* units, including 36 market rate units and 286 income-restricted units (units in which tenancy is limited to low-income or very-low income households). Tenants in roughly half (144) of the 286 income-restricted units also received some form of rental payment assistance such as a Section 8 Voucher. Figure 3 below summarizes tenant incomes as a percentage of area median income (AMI) (adjusted for household size) for all restricted units and for the subset of restricted units in which tenants *did not* receive rental payment assistance. The table shows that the projects have very “deep” income targeting (an average of 32% of AMI) and that tenants without rental assistance tend to have slightly higher incomes (an average of 39% of AMI). Given the relatively small size of the rent roll sample, ICF also asked VHFA to help verify these findings by providing an electronic data file covering over 1,500 units that were jointly funded by VHFA and VHCB. This data file showed an average AMI of 36%.

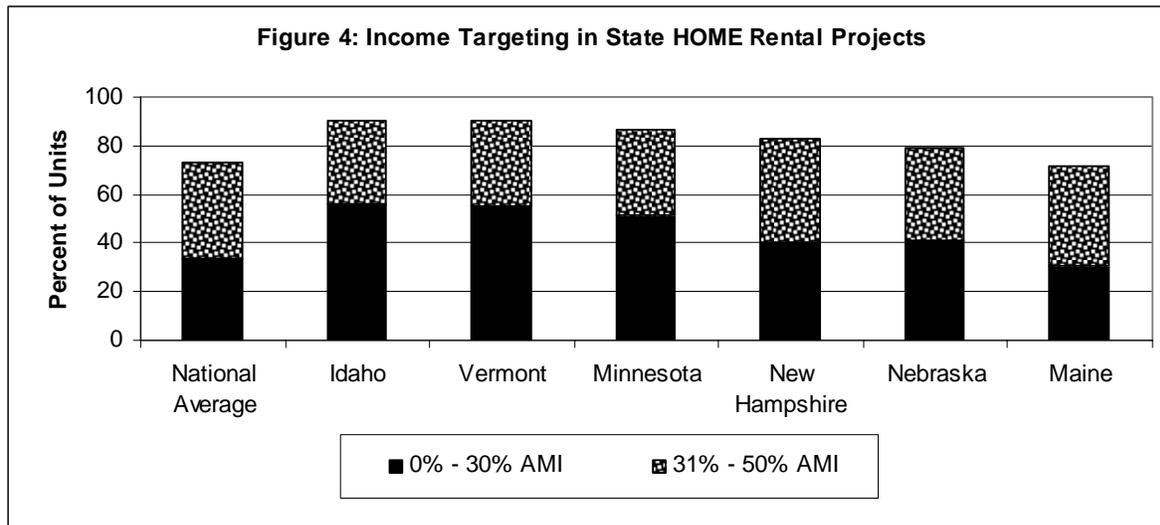
<sup>2</sup> Rent rolls showed the most recently available occupancy data for projects including: household income, household income as a percentage of area median income (adjusted for household size), tenant rental payment, utility payment (if tenant paid), and an indication of whether the tenant received some form of rental payment assistance (e.g., Section 8). The VHFA sample covered 1,500 units that received funding from both VHFA and from VHCB.

**Figure 3: Average Tenant Income as a Percentage of AMI**

	Average AMI	Median AMI
<b>All Income-Restricted Units in ICF Rent Roll Sample</b>	32%	31%
<b>Income-Restricted Units in ICF Rent Roll Sample without Rental Assistance</b>	39%	39%
<b>VHFA Sample of 1,500 Units With Joint VFHA/VHCB Funding</b>	36%	31%

Source: ICF Sample of Project Rent Rolls and VHFA Sample Data

In order to compare Vermont’s income targeting to affordable housing programs in other states, ICF obtained administrative data from HUD on HOME-funded rental housing projects for Vermont, five other states, and national averages for all state HOME-funded rental projects.<sup>3</sup> As Figure 4 shows, Vermont’s HOME-funded projects are targeted much deeper than the national averages in terms of households below 50% of AMI (90.1% of units for Vermont vs. 73.4% of units nationally) and households below 30% of AMI (55.6% of units for Vermont vs. 33.6% of units nationally). In comparison to its regional peers, Vermont is targeting somewhat more deeply than New Hampshire and significantly deeper than Maine. Of the three other rural states for which ICF obtained data (MN, ID, and NE), only Idaho matched the depth of Vermont’s income targeting.



<sup>3</sup> Note that the HUD administrative data, which is drawn from the Integrated Disbursement and Information System (IDIS), has several key differences from the rent roll data: (1) the IDIS data includes all HOME-funded rental projects (not just the 14 projects for which rent rolls were provided); (2) the IDIS data provides income data on *initial occupancy* as opposed to current occupancy; and (3) the IDIS data indicates only whether a household’s income fell into a certain band (e.g., 0-30% AMI) rather than the actual income of the household. ICF selected comparison states based on rural character and/or regional proximity.

## 2.2 Project Development Practices

ICF also evaluated the professionalism and effectiveness of the nonprofits' project development practices. ICF found that the nonprofits are producing a high quality product and using state of art development practices.

- ❑ **Appraisals.** 30 of the 36 studied projects (83%) obtained appraisals prior to final execution of the acquisition contract. For the 30 projects with appraisals, ICF compared appraised value to actual acquisition cost. In only two cases did the acquisition cost exceed the appraised value of the property. Both of these cases involved significant time delays between the time of the appraisal and the time of purchase and yet had only minor appraisal gaps.<sup>4</sup> In many cases acquisitions were at a significant discount—on average acquisitions were made for 79% of appraised value. Of the 6 projects without appraisals, two involved projects in which land was leased to the nonprofit at highly advantageous terms (99 year lease at \$1 per year), one involved donated land, one project involved acquisition at auction, one project involved the construction of additional units on a property already owned by the nonprofit, and nonprofit staff were unable to locate an appraisal for one project initiated in 1999 (Rutland Scattered Site Rehab).
- ❑ **Cost Estimating.** Third party cost estimates for construction expenses are standard practice. As noted later, performance in terms of cost escalation, the difference between the initially budgeted and designed project versus the final cost to build, was evaluated favorably (see page 17).
- ❑ **Market Studies.** Surprisingly, market studies were performed for only 20 of the 36 projects. This finding is somewhat mitigated by the fact that several of the projects without market studies are for special needs populations and/or in areas where a regional market analysis has recently been conducted. Several other of the projects without market studies are small rehabilitation projects so they are brought on line as higher quality housing than prior to renovation. In such cases market studies may be less crucial. VHFA now requires market studies on all Low Income Housing Tax Credit projects.
- ❑ **Quality of Housing Product.** While not a formal element of this evaluation's scope, the ICF team did visit most of the 36 projects to get a sense of construction quality. Generally team members found that the completed projects are of very high quality: construction quality was high; design quality was properly balanced with affordability; and units were both attractive and compatible with their neighborhood characteristics.
- ❑ **Procurement.** ICF reviewed all major procurements for the 36 studied projects and found that groups are properly following written procurement guidelines by soliciting competitive bids and selecting the low bidder.
- ❑ **Timeliness of Completion.** The averaged elapsed time from project start to completion for the 36 studied projects was 2.1 years. In ICF's opinion, based on

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<sup>4</sup> One of these projects had a seven month lag between the appraisal and the closing date (appraised at \$55,000 and acquired for \$57,500, a gap of 5%). The other project had a lag of more than two years due to litigation (appraised at \$855,000 and acquired for \$875,000, a gap of 2%).

experience with affordable housing projects in other states and factoring in the challenging nature of the studied projects, this represents high performance.

## 2.3 Analysis of Development Costs

ICF's analysis of project costs has three elements:

- ❑ A discussion of key factors that influence development costs,
- ❑ A detailed examination of overall development costs and key cost components, and
- ❑ A comparison of observed development costs to other cost benchmarks.

Given the variation among projects discussed in the introduction (e.g., time, number of units, construction type) readers are cautioned about making predictive or system-wide generalizations about costs based on this non-random sample.

### 2.3.1 Factors Affecting Development Costs

The costs examined in the following pages are a function of the development environment within which the 36 studied projects took place, and it is important for readers to understand the following key factors that influence development in Vermont:

- ❑ Regulatory. Vermont's regulatory and social climate towards residential real estate development may be the most restrictive in the United States. By State law, there are no development-by-right parcels. Although a property may be zoned to accept, for example 22 units, after a generally long and difficult local and State review process, the developer may be allowed 14 units on the 22-unit site. In most states, if you purchase an appropriately zoned property, follow the basic guidelines for setting up the properties and have access to water and sewer, you may build by-right without public comment or appeal. The marketplace in those states decides if the product is acceptable.
- ❑ Physical. The physical environment is also challenging. The rocky substrate does not allow for easy and quick on-site sewage disposal. Regrading is difficult and expensive. Much of the land is conserved for natural uses; as a result, inexpensive, easy-to-develop land is a relatively scarce commodity in this rural State. The long winters impact the timing of some aspects of construction and winter construction can add costs. Also, the rural nature of the State contributes to the labor shortage during periods of high building activity.
- ❑ Labor and Material. There are highly qualified carpenters and trades people in Vermont, but the developers ICF spoke with noted that these professionals are typically engaged in the renovation and construction of very expensive retirement, vacation and second homes for the "new money" arrivals to the State. This creates a significant skilled labor shortage for moderately priced homes. In addition, workers' compensation insurance rates are 23% higher than the weighted national average of 16.2%.<sup>5</sup> This tight labor market has a tendency to drive up the price of all moderately

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<sup>5</sup> Source: Means Cost Data 2004.

priced construction projects. Materials may offer some cost advantage in lumber prices due to the proximity to the Canadian border. As U.S. and Canadian officials spar over various duties on lumber, the prices vary dramatically. In general, lumber is less expensive in Vermont than in other states.

- **Residential Pattern.** Vermont is a rural state of small cities and numerous “villages”. The 10 largest cities range from Burlington with 38,900 to Barre with 9,300 (2000 Census). For housing development, this typically translates into small to medium-sized developments. The size of the 36 studied projects is skewed toward smaller projects with projects containing fewer than 20 units comprising 42% (15/36) of the sample. All housing development, especially tax credit projects with their higher level of associated soft costs, benefits from scale in terms of reduced per unit opportunity cost of land, construction and soft costs. Based on experience, ICF believes that a project size of approximately 40 or more units is a break point for efficiency of scale, a size achieved by only 25% of the sample (8/36).

In addition to these general factors, which influence all housing development in Vermont, the studied projects also had to satisfy mission driven priorities as articulated in the Consolidated Plan and VHCB statute (see Figure 2 on page seven for the applicability of these priorities to the 36 studied projects). These mission factors, such as historic preservation and lead paint hazard reduction, have a significant impact on project costs. For example, a 2000 study prepared for VHFA and Housing Vermont found that multiple community development (i.e., non-shelter) objectives, can add up to 40% to the typical cost per square foot.<sup>6</sup>

Of course these Consolidated Plan priorities also have associated benefits, some of which are more easily quantifiable (e.g., the return of a vacant downtown property to property tax rolls) than others (e.g., the spin-off economic benefits from having the same property no longer detracting from downtown districts). Perhaps the most striking quantifiable benefit is the incorporation, through coordination between VHCB and the Agency for Human Services (AHS), of services that allow individuals who were formerly cared for in State hospitals or other institutions to be housed in supportive housing projects. According to interviews with AHS staff, by avoiding longer hospital stays that cost approximately \$900 per day, not only do such projects improve post discharge outcomes for the affected individuals (including reducing the incidence of re-admittance), but the State also realizes significant cost savings, reportedly up to \$800 per day per assisted individual. Significant cost savings also were demonstrated by Cathedral Square, in comparing the costs of an Affordable Assisted Living Residence (AALR) to a Nursing Home Facility (\$121,568 annually in savings, \$68,525 to the State government and \$53,034 to the federal government).

### **2.3.2 Development Costs of Studied Projects**

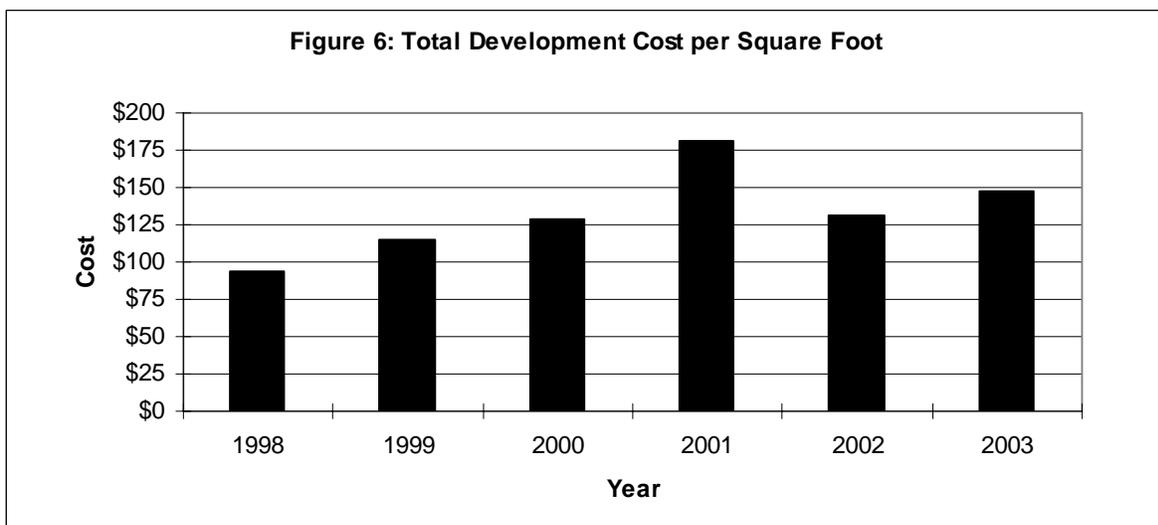
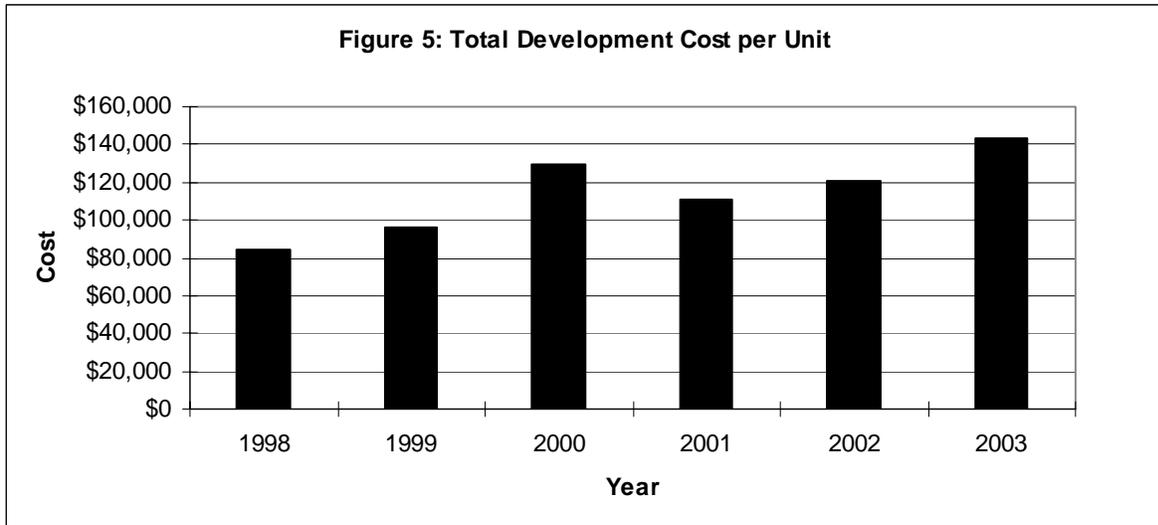
#### **Total Development Costs for the 36 Studied Projects**

Figures 5 and 6 show the average total development costs, on a per unit and square footage basis, for projects in the period 1998-2003. Given the small sample size, readers

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<sup>6</sup> See Housing Development Costs in Vermont; Capital Needs Unlimited, Inc.; April 30, 2000.

are cautioned about making direct comparisons of “average” costs from year to year.<sup>7</sup> One generalization that can be made with a reasonable degree of confidence is that development costs have been increasing. Between 1998-2003, per unit costs of the studied projects increased by 71% (11% annualized) and the square footage costs increased 58% (9.5% annualized).



The total development costs and rate of cost escalation for the projects studied are generally in line with the costs found in the VHCBC Cost Memo. For this review’s studied projects, costs per square foot ranged from \$94 in 1998 up to \$148 in 2003. These figures

<sup>7</sup> For example, the chart showing average square footage costs by year shows a large *apparent* increase in costs between 2000-2001, followed by an almost equally large decrease in costs between 2001-2002. This anomaly is most likely a function of the sampling rules, which selected only two 2001 projects for which square footage costs were available, each of which had above average square footage costs (Copely and Bus Barns).

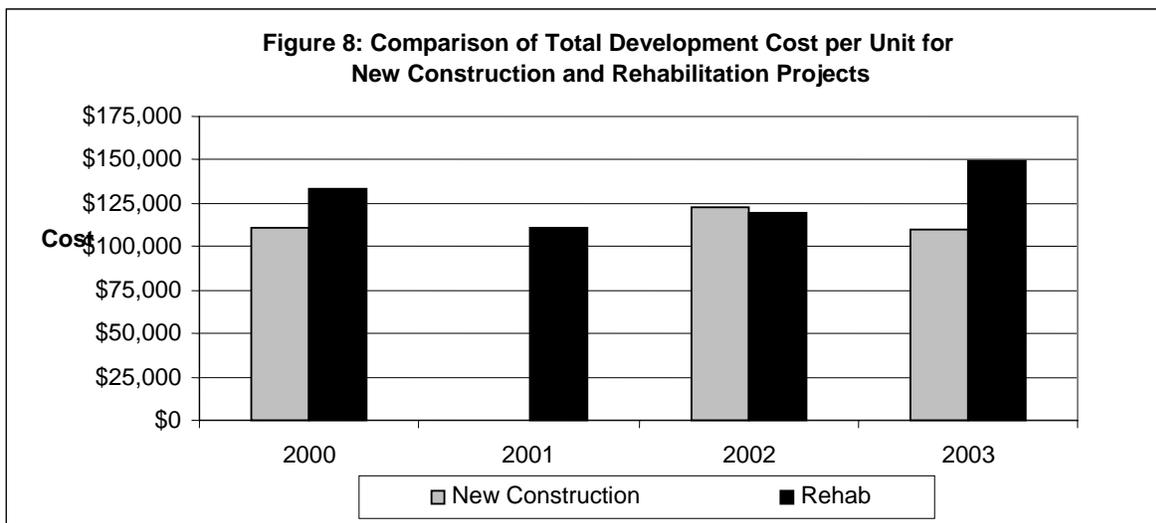
Note: The sponsor of a third 2001 project (Rutland Rehab), with a low per unit cost of \$77,832, was unable to provide a total square footage figure for this project.

are supported by the VHCB Cost Memo, which comprises all VHCB funded rental development projects, with square foot averages increasing from \$93 in 1998 to \$145 in 2003 (projected). On a per unit basis, costs of the studied projects ranged from \$83,989 per unit in 1998 to \$143,384 in 2003. The VHCB Cost Memo shows an increase from \$86,077 to \$147,057 over the same period.

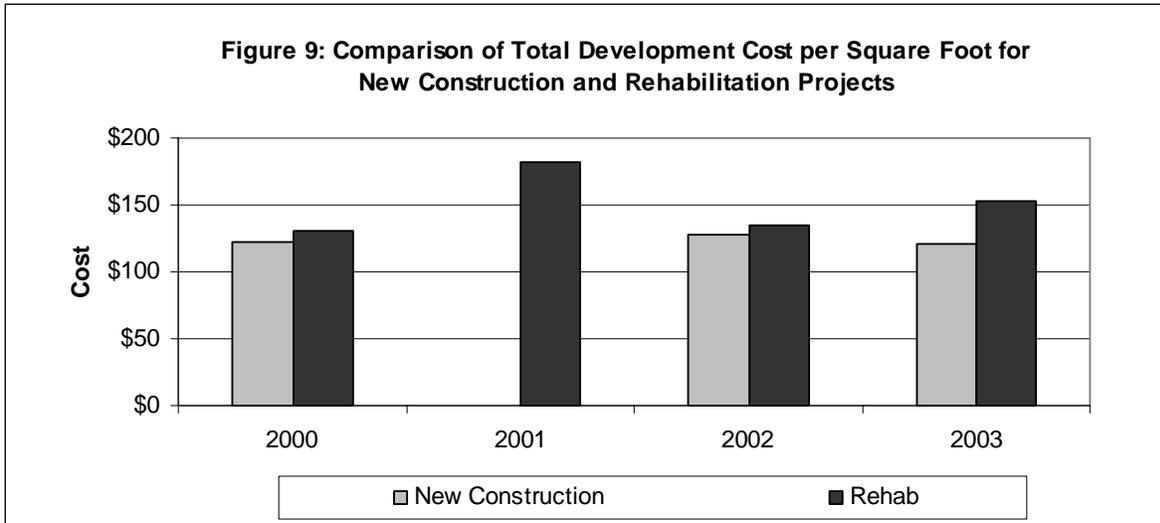
**Figure 7: Comparison of Observed Costs and VHCB Cost Memo**

	Management Review Study Sample per unit	VHCB Cost Memo per unit	Management Review Study Sample per sq. ft.	VHCB Cost Memo per sq. ft.
1998	\$83,989	\$86,077	\$94	\$93
1999	\$96,351	\$101,157	\$115	\$131
2000	\$121,985	\$111,466	\$129	\$117
2001	\$110,445	\$130,339	\$182	\$148
2002	\$120,773	\$144,203	\$131	\$148
2003	\$143,384	\$147,857	\$148	\$145

Comparisons of the total development cost of rehabilitation projects versus new construction projects (see Figures 8 and 9) suggest that rehabilitation projects tend to be more expensive than new construction. However, given the small number of new construction projects included in the study sample<sup>8</sup>, these figures are especially prone to distortion by individual projects that may not accurately reflect typical new construction costs. The VHCB Cost Memo found that, depending on the particular projects in that year's sample, the average cost of the rehabilitation projects is higher than new construction in some years and lower in other years.

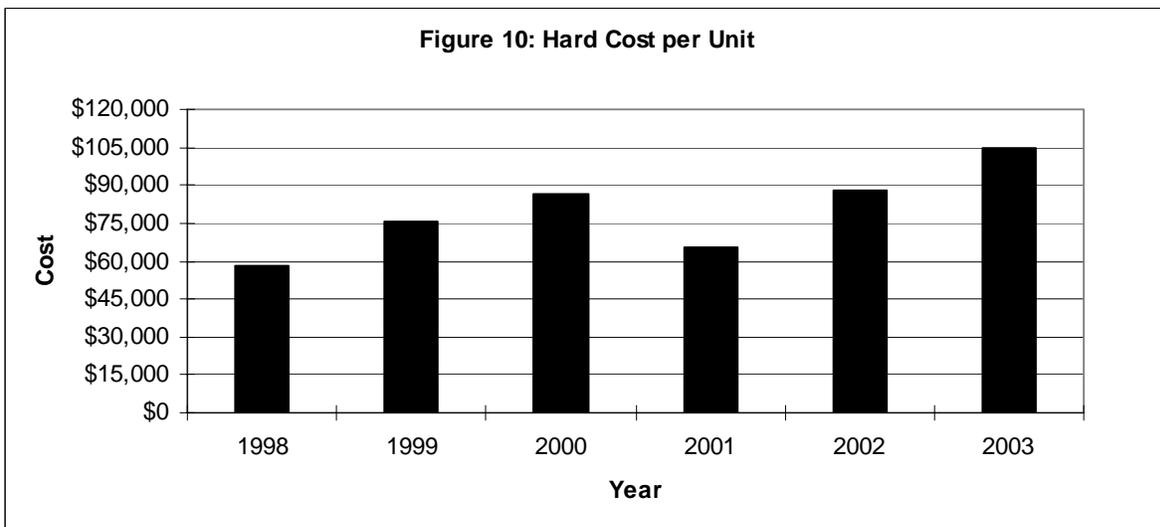


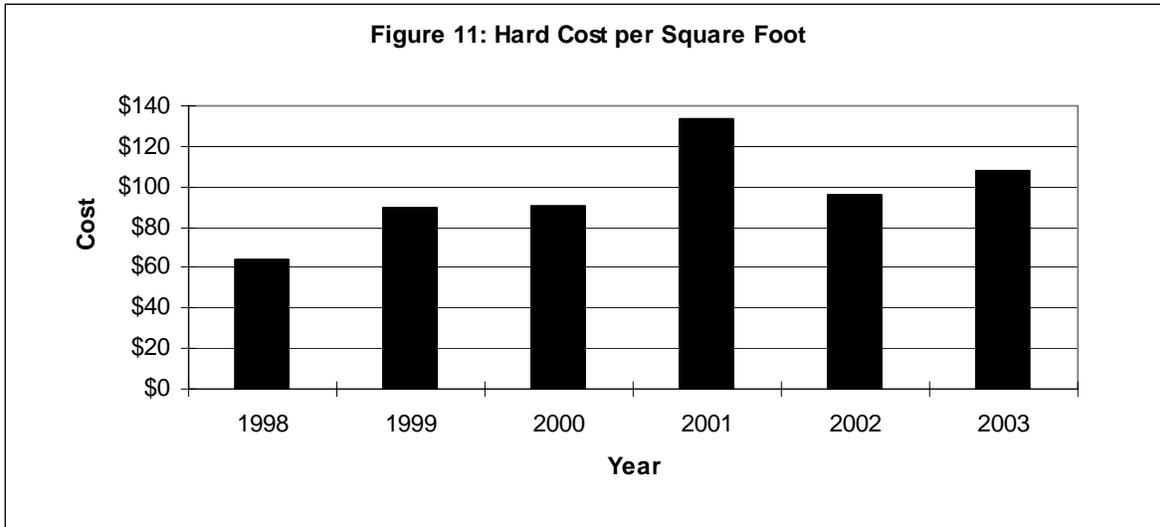
<sup>8</sup> The sample includes one new construction project in 2003, three in 2002, zero in 2001, and one in 2000.



In addition to total development costs, ICF examined the following cost components:

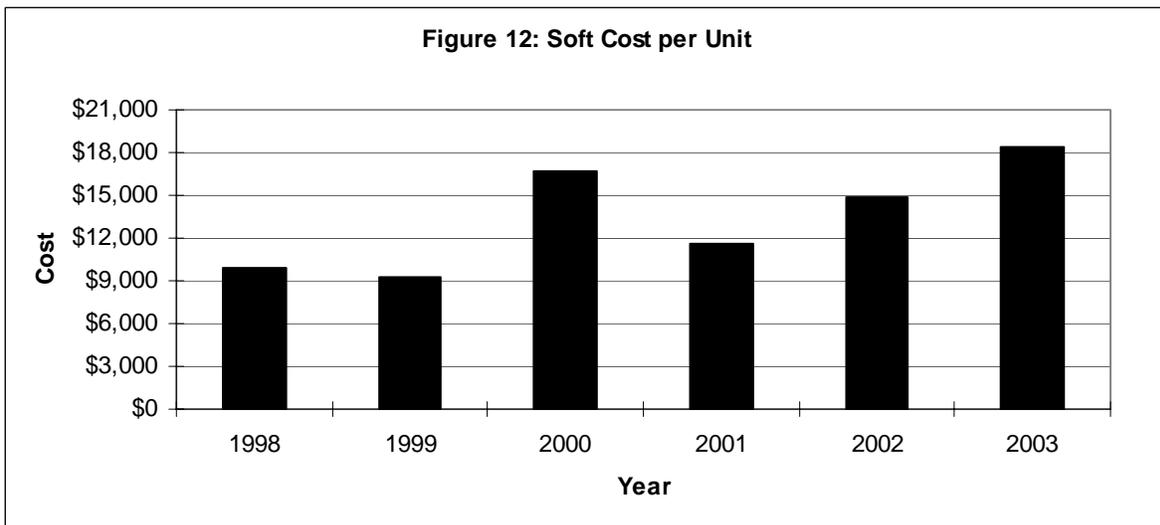
- ❑ **Hard Costs.** On average, hard costs account for 70.2% of total project costs. Figures 10 and 11 show average hard costs per unit and per square foot from 1998-2003. Hard costs have escalated significantly in recent years. Between 1998-2003, per unit hard costs of the studied projects increased by 81% (13% annualized) from \$57,988 to \$104,956. The square footage hard costs increased 68% (12.6% annualized) from \$63.80 to \$107.59. The VHCB Cost Memo, which looked at projects from 1997 to 2004, found a comparable escalation—12.97% annually on a per unit basis and 9.7% annually on a square footage basis. It is important to note that hard costs are generated by a freely operating market, and once a project is defined (i.e., specifications are made), are not controllable by the developers. The developers put their project, as conceived, up for bid using appropriate bidding processes, then award contracts based on the bids.

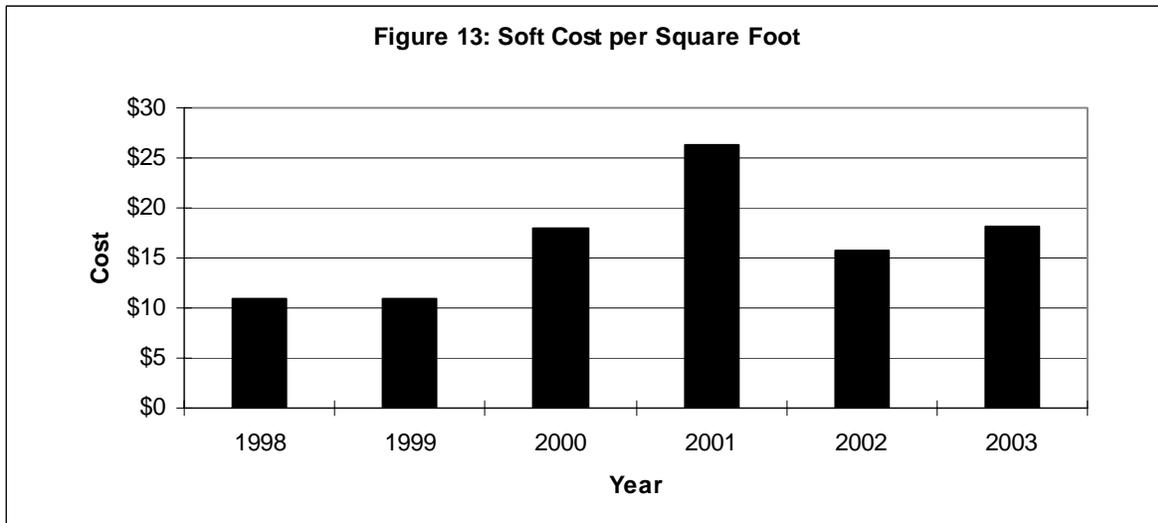




❑ **Soft Costs.** Soft costs are the professional costs of acquiring, designing, contracting out, holding the property, and addressing regulatory requirements during the development period including any development fees for the development partner and the prime developer. Total soft costs for this study sample, excluding developer fees (which are examined separately below in Figures 12 and 13), comprise an average of 11.6% of total development costs. As a point of comparison, based on the ICF project team’s experience with other state programs, we estimate that average soft costs on comparable projects exceed 12% of construction costs.

As with hard costs, soft costs have escalated significantly in recent years. Between 1998-2003, per unit soft costs of the studied projects increased by 85% (13.1% annualized) from \$9,958 to \$18,401. The square footage soft costs increased 66% (10.7% annualized) from \$10.96 to \$18.21. The VHCB Cost Memo, which looked at projects from 1997 to 2004, found a comparable escalation—14% annually on a per unit basis and 10.7% annually on a square footage basis. In ICF’s opinion, the level of studied soft costs are reasonable, especially when factoring in the extensive public appeals and multiple permit reviews that are standard operating procedure in Vermont.





- ❑ **Developer Fee.** The average development fee in the study sample is 7.1% (median = 7.4%). This number is more than one-third lower than the 15% that is allowed by tax credit underwriting. Based on our experience, ICF believes a nonprofit developer fee of 10-15% is a typical figure throughout the United States. In our interviews, in-State private sector developers stated an expectation to garner fees and profit of at least 25%. This is an especially significant difference when considering that the nonprofit fee is used to support an organization whose mission, by law, is typically to develop opportunities for affordable housing. The private sector developer has no such defined mission for the use of funds. In addition, it should be noted that for projects in which a local nonprofit partners with Housing Vermont, development fees are typically split between the two organizations (see Section 5 for more on this practice).
- ❑ **Acquisition Costs.** Averaging 12.7% of total development costs, acquisition costs varied substantially across projects, ranging from 0% (donated land) to 54.5% (mobile home park project). As noted earlier, the groups have leveraged their nonprofit status, mission-driven approach and ability to accept tax-deductible charitable donations to acquire properties at an average of 79% of appraised value.
- ❑ **Design Cost Escalation.** We define design cost escalation as the difference between the initially budgeted and designed project versus the final cost to build, including change orders. Averaging 4.2%, design escalation in the Vermont projects is low. While a few jobs required major design modifications after either approvals or construction start, predominately the projects are easily within contingency ranges. This finding is especially positive due to the requirement to submit financial requests well before the final contract documents have been developed. The very long and invasive local and State permit process could easily eliminate 10% of the units, or require additional parking. In one nonprofit project in Stowe Vermont, the purchase and sales agreement was executed on May 15, 2000. The approval process was started May 16, 2000. A local zoning permit was denied. An appeal was heard in the environmental court in July 2003 and on April 30, 2004, the appeal was denied. With continuous and complete follow-through by the sponsor, the project remains unapproved as of this date, more than four years after it initiated permit approvals. The project is currently being redesigned and is unlikely to be built for another year.

### 2.3.3 Cost Comparisons

This section provides several comparison points for the observed costs. It begins with a comparison of observed costs to a hypothetical project based on a national cost estimating database. The section also provides comparison data for actual rental projects built elsewhere in the region.

#### Comparison to Vermont-Adjusted HomeTech Projected Costs

This section examines the costs of a hypothetical project in Vermont as projected by a nationally derived cost database, the HomeTech Cost Estimating System 2004. To augment the HomeTech data, the example also incorporates cost projections from other reliable sources.

The sample project is a conversion of a single-family dwelling into 3 rental units. This 3-unit contains 900 square feet per dwelling unit, plus 300 additional square feet of common space. The database calculates a \$48,000 opportunity cost plus \$52 a square foot. This results in a total construction contract of \$204,000 or \$68,000 per unit and a corresponding base \$68 per square foot cost for base hard costs. To these numbers the example adds the cost of governmental requirements and mission-driven enhancements to create an appropriate comparison with Vermont affordable housing projects.

- ❑ Historic Requirement. The majority of rehabilitation projects that were investigated were reviewed by the State Historic Preservation Officer and a predominant number fell under Federal Historic Preservation Guidelines. A study performed in 1998 suggested that the Vermont cost of conformance to the Historic Tax Credit Guidelines averaged \$5,900 per unit. If we use the construction industry historical cost index as provided by Means Cost Data 2004 to normalize these figures, the adjustment is 47%. The current historic requirement cost would be \$8,670 per unit.<sup>9</sup>
- ❑ Lead Requirement. Lead hazard reduction is required in all federally funded projects that involve properties constructed prior to January 1, 1978. When the federal subsidy or rehab hard costs exceed \$25,000 per unit, abatement of the lead is required. Abatement is a treatment with at least a 20-year design life. Most of Vermont's housing stock from the pre-1950 period is thoroughly contaminated with lead paint. Lead abatement costs vary widely depending on the extent of contamination and selected intervention. In a 3,000-unit study by the National Center for Lead-Safe Housing, abatement costs ranged from \$8,000 to \$55,000 per unit. The authors estimate that lead abatement in Vermont could range between \$12,000 and \$17,000 per unit with a \$14,500 average.
- ❑ Maximum Energy Efficiency. As part of its mission and as a service to their low-income occupants, all developments strive for Energy Star and/or Model Energy Code performance.<sup>10</sup> This results in very sophisticated, efficient central boiler systems with

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<sup>9</sup> Satisfying historic preservation requirements, while adding costs, also makes properties eligible for federal Historic Rehabilitation Tax Credits (RTCs) that can help offset some of the additional costs.

<sup>10</sup> VHCB and VHFA's joint *Policy on the Conservation of Energy and Water in Residential Properties* requires that developers "select designs and systems with consideration of economy, future flexibility, operation and maintenance costs, and impact on the environment, including potential use of renewable resources." While this policy generally increases construction costs, it translates into reduced operating costs, which, over the life of the property, more than compensate for the higher upfront costs. In addition, energy efficient properties are

multiple distribution using sophisticated controls and variable speed motors. The initial installed cost of these systems is easily twice that of an individual gas, forced air unit for each apartment. Energy efficiency measures to meet and/or exceed the Model Energy Code are estimated to cost in our typical 3-flat building an additional \$26,000 or \$8,666 per unit.

- ❑ Reconfiguration for Additional Units. Reconfiguration to the max is the norm in adaptive reuse and whole house conversions. A profit-motivated developer would avoid renovating certain spaces because the per square foot development cost is dramatically higher than the other easier spaces. Because adding additional units is such a high priority for the system, the nonprofit developers and their architects consistently maximize the unit count while utilizing attic and loft-type spaces to become additional living units. We estimate that this translates into a 4% increase in per-unit costs.
- ❑ Final Calculation. Starting from a \$68,000 per unit base hard cost of construction contract and adding \$8,670 per unit for historic requirements, \$14,500 for lead abatement, \$8,666 for energy efficiency, and \$2,720 for extensive reconfiguration costs (4%), results in a total comparable construction hard cost of \$102,500 per unit or \$102 per square foot.

<b>Projected Cost Item</b>	
Base Hard Costs	\$68,000
Historic	\$8,670
Energy Efficiency	\$8,666
Unit Reconfiguration	\$2,720
<u>Lead reduction</u>	<u>\$14,500</u>
Total Hard Costs Projected	<b>\$102,500 per unit/ \$102 per sq. ft.</b>
Total Hard Costs VHCB Cost Memo	<b>\$101,500 per unit/ \$99 per sq. ft.</b>
Total Hard Costs ICF Sample (2003)	<b>\$104,956 per unit/ \$107.59 per sq. ft</b>

The total development cost of the hypothetical project ends up being slightly more expensive than the costs in the VHCB Cost Memo and slightly less expensive than the costs of the studied projects.

Vermont Costs Compared to Other Areas

The Federal Home Loan Bank of Boston (FHLB) operates an Affordable Housing Program (AHP) throughout New England that grants 10% of the Banks' net earnings to eligible housing initiatives through a competitive application process. In a memo to the ICF research team, Liz Nickerson of the FHLB reports that the majority of Vermont AHP

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eligible for special utility-sponsored efficiency programs which can help offset the capital costs of energy-efficient technologies.

projects have been co-funded by VHCB. In addition, ICF's review of sources and uses statements showed that AHP was used in support of many of the 36 studied projects. The FHLB provided ICF with information on rental project applications from 2001-2004 (see Figure 14 below). The FHLB data shows that Vermont has the lowest per unit development costs in the region and the second lowest cost on a net square feet basis.

**Figure 14: Comparison of Development Costs of Rental Project Funding Applications Submitted to the Federal Home Loan Bank of Boston (2001-2004)**

	VT	CT	ME	MA	NH	RI	<i>Sample Average</i>
Number of Projects	13 projects	8 projects	8 projects	28 projects	9 projects	7 projects	<i>73 total projects</i>
Average Size	22 units	38 units	21 units	44 units	22 units	65 units	<i>36 units</i>
Average TDC Per Unit	\$136,648	\$141,049	\$163,482	\$212,862	\$163,609	\$152,297	<i>\$174,128</i>
Average Cost Per Net Sq. Ft.	\$153	\$132	\$317	\$284	\$180	\$157	<i>\$223</i>

*Source: Federal Home Loan Bank of Boston, Basic Rental (LIHTC) Applications 2001-2004*

In ICF's interviews with private developers and other stakeholders, it was suggested that New Hampshire is most comparable to Vermont in terms of development environment. As a second regional comparison, ICF obtained data on the New Hampshire Housing Finance Authority's most recent round of approved tax credit projects. Figure 15 below compares the New Hampshire projects to the study sample and the VHCB Cost Memo. It is interesting to note that, while New Hampshire total costs are comparable to Vermont (average TDC of \$162,127 per unit<sup>11</sup>), hard cost per square foot averages (*not including contingencies*) are \$76 for rehab and \$98 for new construction, lower than those for Vermont. This difference suggests that the other components of total cost are higher in New Hampshire.

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<sup>11</sup> These figures are based on projects recommended for award in NHHFA's 2004 LIHTC first round. Note the severe limitations on the predictive ability of these data: that these costs are as proposed in the sponsor's application (i.e., not actuals) and they are drawn from the small sample of four projects recommended for approval in Round 1.

**Figure 15: Comparison of Costs with Recent New Hampshire Tax Credit Approvals**

	<b>Study Sample 2003</b>	<b>VHCB Cost Memo 2004*</b>	<b>New Hampshire 2004</b>
TDC per unit	\$143,348	\$155,304	\$162,127
TDC per sq ft	\$148	\$157	not available
Hard cost per sq ft rehab	\$111	\$88	\$76
Hard cost per sq ft new construction	\$88	\$100	\$98

\* Numbers are weighted averages. *Source: NH HFA Funding Documents*

### Nonprofit Development Compared to For-Profit

Comparisons with the private sector in Vermont are particularly difficult, mainly due to the differences between the type of projects being built by private sector developers and those projects being built by the studied nonprofits. One private developer who asked not to be named in print provided information that showed base per unit development costs on multi-family structures of \$138,000 per unit before fees and profit, with an anticipated sale price of \$180,000 per unit. Other private developers that ICF contacted were unwilling to share cost information or developed very different housing products that are not comparable to the studied projects (e.g., single-family homes selling for over \$300,000). Interviews with private sector Vermont developers did reveal that they are grappling with some of the same cost challenges. For example, developers stated that labor shortages and the time consuming permitting process would continue to escalate costs.

A number of the studied projects were originally undertaken then abandoned by the private sector due to the inordinate difficulty of the project or the cost and difficulty of maintaining permanent affordability, including the following examples:

- The Bus Barns project in Burlington. This project is now a mixed-use historic space with accessible affordable housing, attractive streetscape, and commercial space. The private sector alternative for the site was a rent-a-truck lot.
- Park Place in downtown Burlington. This was a burned out, boarded up building. The private sector developer encountered ongoing problems with design, permitting and cost, and requested the nonprofit's help to come in and take over the project – now an attractive combination of commercial and housing space.

In ICF's opinion, projects such as those above, which are a direct manifestation of the Consolidated Plan priorities, will only attract mission-driven nonprofits. There is simply too much risk and not enough reward to attract private developers who have other development opportunities available.

Considering the factors affecting development, the professionalism of the processes used to control costs, and the costs of the projects studied in comparison to other cost benchmarks areas, ICF concludes that the cost for Vermont projects studied is well-managed and within, or, in some cases, below expectations.

## 3.0 Nonprofit Management

The nonprofit management section begins with a summation of survey results from the management systems sections of the organizational questionnaires and is followed by an analysis of financial statement information. The section concludes with a discussion of a key issue for the nonprofit system—property and asset management.

### 3.1 Management Systems

Prior to site visits, ICF sent each nonprofit organization a questionnaire which gathered specific data points on organizational and management systems, asked nonprofits a series of open-ended self-assessment questions (e.g., organizational strengths/weakness, development climate), and solicited a number of organizational documents including five years of audits. Key findings with respect to management systems include the following:

- ❑ **Strategic/Business Plan:** Seven of the nine nonprofits have either a formal strategic plan or business plan, and one other (GHT) is currently developing one.
- ❑ **Asset Management Plan:** Only three nonprofits have a formal asset management plan (GHT, CSC, HV). However, one of the three, Housing Vermont, provides asset management services for projects where it is a partner. This is an important distinction, since Housing Vermont has a sophisticated, quantifiable system for doing quarterly evaluations of each property, and, where appropriate, for putting properties on their “watch list.” It is important to note that seven of the eight nonprofits in the study (other than Housing Vermont) had projects in which Housing Vermont was a partner, and 19 of the 36 projects involve Housing Vermont as a partner. This may explain, in part, why more groups do not have formal asset management plans.
- ❑ **Fund Accounting:** All the nonprofits, except Housing Vermont, which, given their unique role, tracks by individual project, has a fund accounting system. Five of the nine use MIP software.

Of the audit reports that were provided to ICF, only one organization had any formal audit findings, and even those were for relatively minor issues (e.g., cash escrowed in excess of the \$100,000 federally insured amount), which have since been resolved.

ICF also briefly reviewed nonprofit board minutes from the last two meetings for each organization. The minutes provided an adequate accounting of board decisions and indicated a proper level of engagement by the boards.

### 3.2 Analysis of Financial Indicators

ICF used an analytical template developed by the Enterprise Foundation to examine nonprofit financial performance for indications of organizational well being. A companion guide to the template, *Assessing Your Organization's Finances*, suggests desired ranges for each of the analytical indicators contained in the template. To assist organizations in completing the template, ICF mailed each organization a copy of the companion guide and

provided guidance to the accountants for each organization. Findings, which cover the years 2001-2003, include the following:

- ❑ **Operational Soundness:** As a simple measure organizational soundness, ICF looked at organizational deficit ratios – the relationship of total revenue to expenses<sup>12</sup>. The desired range for this benchmark, as established by the Enterprise Foundation, was any ratio greater than zero. All nine organizations had positive three-year averages (dollar weighted), but two groups had negative ratios for 2003. These two organizations, GHT and LHP, should be monitored carefully going forward. See Figure 16 below for further detail. It is important to note that there are significant fluctuations for an organization from one year to the next depending on investment decisions, unanticipated changes in operating or capital costs on projects, and delays in project completions which can push anticipated developer fees from one operating year into another.

**Figure 16: Operational Soundness**

	YEAR ONE			YEAR TWO			YEAR THREE			
	Total Revenue	Total Expenses	Deficit Ratio	Total Revenue	Total Expenses	Deficit Ratio	Total Revenue	Total Expenses	Deficit Ratio	3 year Average
BCLT	\$1,923,681	\$1,836,155	5%	\$2,326,597	\$2,007,233	16%	\$2,630,854	\$2,432,178	8%	10%
GHT	\$1,208,698	\$1,107,483	9%	\$1,817,426	\$1,257,300	45%	\$807,577	\$884,447	-9%	18%
RAHC	\$831,524	\$673,368	23%	\$785,920	\$777,972	1%	\$803,021	\$783,981	2%	8%
BACLT	\$798,969	\$777,663	3%	\$937,612	\$838,754	12%	\$1,079,056	\$835,111	29%	15%
LHP	\$203,625	\$159,184	28%	\$315,757	\$195,951	61%	\$191,975	\$227,062	-15%	22%
LCHDC	\$3,044,027	\$2,776,855	10%	\$3,410,157	\$3,160,910	8%	\$3,266,106	\$3,192,486	2%	6%
RCCLT	\$746,191	\$639,047	17%	\$708,141	\$666,400	6%	\$847,758	\$748,542	13%	12%
CS	\$1,293,580	\$1,276,661	1%	\$1,928,212	\$1,650,129	17%	\$1,624,575	\$1,607,186	1%	7%
HV	\$1,285,106	\$1,211,647	6%	\$1,547,098	\$1,369,235	13%	\$1,980,575	\$1,653,454	20%	14%

The development business requires organizations to incur large expenses over extended periods of time during the development phase of a project. Grants for projects are received in large chunks. Therefore large fluctuations are not unusual. Ongoing shortfalls, however, should be monitored as suggested above.

- ❑ **Control:** This indicator assesses the extent to which organizations have short-term managerial control over their revenue streams. It has two components. The first is the ratio of receivables to current assets. The desired range is less than 25%. Seven of nine organizations were consistently below 25% (intra-company loans were excluded). The two organizations with higher ratios stated that the overage was due to receivable developer fees – a common feature of rental housing projects. See Figure 17 below for further detail.

<sup>12</sup> Defined as [(total revenues – total expenses)/total expenses].

**Figure 17: Control, Accounts Receivable**

	END OF YEAR ONE			END OF YEAR TWO			END OF YEAR THREE			
	Accounts Receivable	Total Current Assets	Ratio	Accounts Receivable	Total Current Assets	Ratio	Accounts Receivable	Total Current Assets	Ratio	3 Year Average
BCLT	\$117,634	\$2,541,181	5%	\$172,551	\$2,055,939	8%	\$104,757	\$2,156,006	5%	6%
GHT	\$46,638	\$291,625	16%	\$65,473	\$339,062	19%	\$51,895	\$259,138	20%	18%
RAHC	\$53,046	\$336,799	16%	\$31,256	\$318,888	10%	\$13,714	\$296,307	5%	10%
BACLT	\$26,892	\$321,964	8%	\$25,650	\$452,193	6%	\$17,791	\$597,421	3%	5%
LHP	\$3,637	\$168,571	2%	\$12,968	\$464,895	3%	\$6,599	\$393,055	2%	2%
LCHDC	\$105,684	\$1,209,715	9%	\$283,065	\$1,418,757	20%	\$250,167	\$1,395,260	18%	16%
RCCLT	\$32,318	\$244,388	13%	\$29,171	\$295,430	10%	\$21,370	\$222,732	10%	11%
CSCC	\$113,562	\$499,481	23%	\$174,597	\$758,929	23%	\$204,051	\$659,477	31%	26%
HV	\$1,090,050	\$2,345,772	46%	\$1,557,233	\$4,645,054	34%	\$1,496,606	\$5,309,366	28%	34%

The other control measure is the ratio of unrestricted funds to total revenue with a desired range of more than 25%. The term “unrestricted funds,” means funds that can be used for any legitimate purpose by the organization, whereas restricted funds can be used only for defined purposes. A higher percentage of unrestricted funds gives an organization more flexibility in its use of revenues. All organizations were well above the target figure.

*A note of caution to readers: the term “unrestricted” used in an accounting sense can be somewhat misleading. Though funds may be technically unrestricted, the major part of these funds is revenue from properties that is needed to sustain those properties.*

**Figure 18: Control, Unrestricted Funds**

	END OF YEAR ONE			END OF YEAR TWO			END OF YEAR THREE			
	Unrestricted Revenue	Total Revenue	Ratio	Unrestricted Revenue	Total Revenue	Ratio	Unrestricted Revenue	Total Revenue	Ratio	3 Year Average
BCLT	\$1,923,681	\$3,107,626	62%	\$2,326,597	\$3,507,476	66%	\$2,630,854	\$4,383,011	60%	63%
GHT	\$1,208,698	\$1,399,948	86%	\$1,817,426	\$2,463,724	74%	\$2,822,206	\$4,428,983	64%	71%
RAHC	\$831,524	\$841,004	99%	\$785,920	\$795,596	99%	\$803,021	\$1,063,703	75%	90%
BACLT	\$771,969	\$798,969	97%	\$892,612	\$937,612	95%	\$992,456	\$1,079,056	92%	94%
LHP	\$106,686	\$203,625	52%	\$225,773	\$315,757	72%	\$101,265	\$191,975	53%	61%
LCHDC	\$2,494,173	\$3,013,777	83%	\$2,993,891	\$3,410,157	88%	\$2,824,554	\$3,266,106	86%	86%
RCCLT	\$755,484	\$755,484	100%	\$708,141	\$708,141	100%	\$847,758	\$847,758	100%	100%
CSC	\$1,263,580	\$1,293,580	98%	\$1,851,344	\$1,928,212	96%	\$1,582,325	\$1,624,575	97%	97%
HV	\$1,285,106	\$1,285,106	100%	\$1,547,098	\$1,547,098	100%	\$1,785,532	\$1,980,575	90%	96%

- Entrepreneurial Orientation:** This indicator evaluates the extent to which an organization is able to garner fee income (e.g., development fees, service fees,

rental/business related income)<sup>13</sup>. The desired benchmark range for this indicator is greater than 20%. All nine organizations exceeded this benchmark in each of the three studied years. See Figure 19 below for further detail.

**Figure 19: Entrepreneurial Orientation**

	END OF YEAR ONE			END OF YEAR TWO			END OF YEAR THREE			
	Revenue From Fees	Total Revenue	Ratio	Revenue From Fees	Total Revenue	Ratio	Revenue From Fees	Total Revenue	Ratio	3 Year Average
BCLT	\$1,295,123	\$3,017,626	43%	\$1,505,916	\$3,507,476	43%	\$1,829,485	\$4,383,011	42%	42%
GHT	\$484,400	\$1,399,948	35%	\$488,188	\$2,463,724	20%	\$932,739	\$4,428,983	21%	23%
RAHC	\$319,717	\$841,004	38%	\$257,606	\$795,596	32%	\$255,638	\$1,063,703	24%	31%
BACLT	\$631,374	\$798,969	79%	\$748,383	\$937,612	80%	\$769,532	\$1,079,056	71%	76%
LHP	\$84,441	\$203,625	41%	\$196,123	\$315,757	62%	\$69,343	\$191,975	36%	49%
LCHDC	\$933,703	\$3,013,777	31%	\$1,437,100	\$3,410,157	42%	\$1,363,194	\$3,266,106	42%	39%
RCCLT	\$487,673	\$746,191	65%	\$474,351	\$708,141	67%	\$586,735	\$847,758	69%	67%
CSC	\$1,248,949	\$1,293,580	97%	\$1,819,014	\$1,928,212	94%	\$1,565,150	\$1,624,575	96%	96%
HV	\$1,101,259	\$1,285,106	86%	\$1,294,716	\$1,547,098	84%	\$1,569,788	\$1,980,575	79%	82%

- Financial Dependency:** These indicators measure the extent to which the organization is financially dependent on single sources of revenue (governmental and foundation)<sup>14</sup>. The desired benchmark for this indicator is less than 40%. Two organizations, LHP and GHT, had three year averages that exceeded the desired range by 3% and 5% respectively. See Figure 20 below for further detail about Governmental Dependency. Foundation dependency was not a significant issue for any organization with a system wide average of just 1% over the three studied years. See Figure 21 below for further detail about Foundation Dependency.

**Figure 20: Governmental Dependency**

	END OF YEAR ONE			END OF YEAR TWO			END OF YEAR THREE			
	Revenue From Government	Total Revenue	Ratio	Revenue From Government	Total Revenue	Ratio	Revenue From Government	Total Revenue	Ratio	3 Year Average
BCLT	\$386,611	\$1,923,681	20%	\$537,769	\$2,326,597	23%	\$342,473	\$2,630,854	13%	18%
GHT	\$559,979	\$1,399,948	40%	\$1,231,778	\$2,463,724	50%	\$1,938,769	\$4,428,983	44%	45%
RAHC	\$41,448	\$841,004	5%	\$35,000	\$795,596	4%	\$40,729	\$1,063,703	4%	4%
BACLT	\$111,076	\$798,969	14%	\$131,721	\$937,612	14%	\$146,623	\$1,079,056	14%	14%
LHP	\$103,051	\$203,625	51%	\$101,310	\$315,757	32%	\$98,734	\$191,975	51%	43%
LCHDC	\$1,078,804	\$3,013,777	36%	\$988,096	\$3,410,157	29%	\$866,021	\$3,266,106	27%	30%
RCCLT	\$239,495	\$746,191	32%	\$200,450	\$708,141	28%	\$232,744	\$847,758	27%	29%
CSC	\$30,000	\$1,293,580	2%	\$76,868	\$1,928,212	4%	\$42,250	\$1,624,575	3%	3%
HV	\$0	\$1,285,106	0%	\$0	\$1,547,098	0%	\$0	\$1,785,532	0%	0%

<sup>13</sup> Defined as fee revenue/total revenue.

<sup>14</sup> Defined as revenue from government/total revenue (or revenue from foundations/total revenue).

**Figure 21: Foundation Dependency**

	END OF YEAR ONE			END OF YEAR TWO			END OF YEAR THREE			
	Revenue From Foundations	Total Revenue	Ratio	Revenue From Foundations	Total Revenue	Ratio	Revenue From Foundations	Total Revenue	Ratio	3 Year Average
BCLT	\$18,053	\$1,923,681	0.9%	\$1,000	\$2,326,597	0.0%	\$128,322	\$2,630,854	4.9%	2.1%
GHT	\$87,950	\$1,399,948	6.3%	\$144,500	\$2,463,724	5.9%	\$166,000	\$4,428,983	3.7%	4.8%
RAHC	\$6,992	\$841,004	0.8%	\$3,220	\$795,596	0.4%	\$246	\$1,063,703	0.0%	0.4%
BACLT	\$23,871	\$798,969	3.0%	\$7,500	\$934,612	0.8%	\$13,100	\$1,079,056	1.2%	1.6%
LHP	\$0	\$203,625	0.0%	\$0	\$315,757	0.0%	\$0	\$191,975	0.0%	0.0%
LCHDC	\$0	\$3,013,777	0.0%	\$0	\$3,410,157	0.0%	\$0	\$3,266,106	0.0%	0.0%
RCCLT	\$1,418	\$746,191	0.2%	\$3,000	\$708,141	0.4%	\$2,500	\$847,758	0.3%	0.3%
CSC	\$0	\$1,293,580	0.0%	\$20,000	\$1,928,212	1.0%	\$0	\$1,624,575	0.0%	0.4%
HV	\$0	\$1,285,106	0.0%	\$0	\$1,547,098	0.0%	\$0	\$1,785,532	0.0%	0.0%

□ **Community Support:** This indicator measures the extent to which the organizations receive financial support from local individuals and institutions<sup>15</sup>. The desired benchmark for this indicator is greater than 5%. Only two of the nine organizations had three year averages that exceeded the desired benchmark, and a third organization was six-tenths of a percent from the desired range. Only Housing Vermont and Cathedral Square, which operate State-wide, reported no local support funds. See Figure 22 below for further detail about Community Financial Support.

**Figure 22: Community Financial Support**

	END OF YEAR ONE			END OF YEAR TWO			END OF YEAR THREE			
	Local Revenue	Total Revenue	Ratio	Local Revenue	Total Revenue	Ratio	Local Revenue	Total Revenue	Ratio	3 Year Average
BCLT	\$114,791	\$1,923,681	6.0%	\$148,474	\$2,326,597	6.4%	\$142,985	\$2,630,854	5.4%	5.9%
GHT	\$41,046	\$1,399,948	2.9%	\$95,294	\$2,463,724	3.9%	\$22,145	\$4,428,983	0.5%	1.9%
RAHC	\$24,110	\$841,004	2.9%	\$22,528	\$795,596	2.8%	\$23,497	\$1,063,703	2.2%	2.6%
BACLT	\$24,452	\$798,969	3.1%	\$29,289	\$1,005,651	2.9%	\$79,982	\$1,219,387	6.6%	4.4%
LHP	\$13,356	\$203,625	6.6%	\$13,300	\$315,757	4.2%	\$16,850	\$191,975	8.8%	6.1%
LCHDC	\$48,000	\$3,013,777	1.6%	\$50,000	\$3,410,157	1.5%	\$50,000	\$3,266,106	1.5%	1.5%
RCCLT	\$11,384	\$746,191	1.5%	\$17,065	\$708,141	2.4%	\$21,297	\$847,758	2.5%	2.2%
CSC	\$0	\$1,293,580	0.0%	\$0	\$1,928,212	0.0%	\$0	\$1,624,575	0.0%	0.0%
HV	\$0	\$1,285,106	0.0%	\$0	\$1,547,098	0.0%	\$0	\$1,785,532	0.0%	0.0%

<sup>15</sup> Defined as revenue from special events and local fundraising/total revenue.

### 3.3 Operating Support Grants

VHCB, per its enabling statute, provides operating support grants to many of the housing nonprofits in the system, including eight of the nine organizations in the study. During our interviews with private sector developers, we heard several variations of a common theme—that nonprofits have high (i.e., inefficient) overhead costs that necessitate these type of operating grants. ICF investigated this concern in two ways: by computing the percentage of annual operating budgets that are supported by operating grants, and by treating operating grants as equivalent to development fees, and recomputing development fees for projects completed during the grant year. ICF examined operating grants for fiscal years 2001-2004.

- ❑ **Operating grants as a percentage of organizational budgets.** System wide<sup>16</sup> in 2004, VHCB reports that operating grants averaged 7.6% of nonprofit operating budgets (with a range from 4.1%-18.1%). For years 2001-2003, ICF’s analysis, which covered only the eight studied nonprofits that received operating grants, showed a comparable level of support. As shown in Figure 23 below, operating support constituted a relatively comparable share of organizational budgets in 2001-2003, with dollar weighted averages ranging from 4.3% to 4.8% of budgets.

**Figure 23: VHCB Operating Support as a Percentage of Operating Budgets**

<u>Organization</u>	<u>2003</u>	<u>2002</u>	<u>2001</u>
BACLT	11.4%	12.3%	13.2%
BCLT	4.7%	4.8%	6.2%
CSC	2.2%	2.1%	2.3%
GHT	6.5%	4.4%	4.5%
LCHDC	1.2%	1.2%	1.3%
LHP	25.3%	32.7%	34.6%
RAHC	7.1%	7.1%	8.7%
RCCLT	6.9%	7.4%	6.8%
<b>Average of Averages</b>	<b>8.2%</b>	<b>9.0%</b>	<b>9.7%</b>
<b>Dollar Weighted Average</b>	<b>4.4%</b>	<b>4.3%</b>	<b>4.8%</b>

- ❑ **Operating grants as an adjunct to developer fee.** Of the 21 studied projects completed between 2001-2004, 19 were developed by a nonprofit that also received operating support. For those 19 projects, ICF added operating support funds to total developer fee to derive an “adjusted developer fee.” The average adjusted developer fee did increase to 8.7% vs. the sample average of 7.1%. Nonetheless, adjusted fees remain relatively low compared a typical nonprofit fee of 10-15%.<sup>17</sup>

<sup>16</sup> In 2004, VHCB made operating grants to 13 organizations, seven of which were included in this study. The 7.6% figure noted above is the average for all 13 organizations; the average for the 7 study organizations in 2004 was 9.6%.

<sup>17</sup> Note that ICF’s analysis did not consider whether developers completed additional projects during a year in which they received operating support (i.e., operating support was factored only into studied projects, rather than being allocated among projects completed during the same year). If developers did complete multiple projects during a year in which they also received operating support, this would mean that “adjusted development fees” were actually lower than those reported above.

As a final observation on the subject of operating grants, ICF notes that the practice of providing operating support to nonprofits is seen in the community development field as a model practice that contributes to organizational performance. In ICF's opinion, VHCB is particularly effective in its use of operating grants—focusing them on key organizational enhancements (e.g., upgrades in accounting software) and using them as a lever to improve management practices in tandem with an active monitoring program.

### **3.4 Organizational Salaries**

As required by the evaluation scope of work, ICF also analyzed a key component of organizational operating costs, staff salaries. ICF's analysis builds off of a January 2003, survey of salaries at the housing nonprofits conducted by Housing Vermont. ICF first verified that that salary survey reflected actual salaries paid at the nonprofits in the study. ICF then compared salary survey data to data from the U.S. Bureau of Labor Statistics (BLS)<sup>18</sup>. ICF confirmed that comparison of salaries to the BLS data was valid by comparing job classification descriptions in the BLS database, which tracks wages in both the for-profit and nonprofit sectors, with the jobs performed at the nonprofits<sup>19</sup>. To the extent there were variances between the two perspectives, the skills needed and complexity of tasks at the nonprofit reflected a higher level than the BLS descriptions. Please note that this comparison is of Vermont nonprofit salaries with those for similar positions throughout Vermont. Comparisons with other states can easily be done by accessing the BLS database on the web.

ICF's analysis, summarized in Figure 24, found that the housing nonprofit salaries are low compared to the Vermont occupational survey ranges. Salaries also fell below the average salaries for New England nonprofit organizations that were designated NeighborWorks Organizations by the Neighborhood Reinvestment Corporation (NRC), as reported by the NRC Research Department (May 2003). The Vermont housing nonprofits salaries were within the expectations of the ICF team based on our experience in other areas.

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<sup>18</sup> In order to preserve confidentiality assurances which were given by the research team to studied nonprofits, salary information is discussed at the system level, rather than organization by organization. Also note that Vermont-specific BLS data is used by the Vermont Department of Employment and Training and is available on their website.

<sup>19</sup> Housing Vermont itself was not included in the survey, but the salaries there also fell below the statewide averages.

**Figure 24: Vermont Salary Comparisons**

	<b>BLS Vermont State Average – May 2003</b>	<b>Average Salary Per January 2003 Survey</b>	<b>Range of Salaries Per January 2003 Survey</b>
<b>Executive Director of Property Real Estate and Community Association</b>	\$91,040	\$50,000	\$40,000-\$61,440
<b>Finance Director</b>	\$89,900	\$35,806	\$23,573- \$59,218
<b>Eligibility Interviewers Government Programs</b>	\$32,060	\$26,000 (Property Manager)	\$25,248- \$45,019 (Property Manager)
<b>Loan Counselors</b>	\$44,620	\$28,896	\$24,079- \$34,320
<b>Construction Managers</b>	\$80,250	\$30,000 (Project manager)	\$30,000- 48,840 (Project manager)

Other studies have found that benefits at housing nonprofits tend to lag the public and private sector, and this may have an impact on job tenure and organizational performance.<sup>20</sup> The main problem organizations experience stemming from low comparable wages is the loss of staff who have gained skills and knowledge of the organization’s activities. Using the BLS figures for the U.S. population as a whole for comparison, the average job tenure for Vermont housing nonprofits is shorter than the national average for all occupations. Average job tenure across all positions reported was 2.75 years. In January 2002, the national job tenure averages for women and men over age 25 were 4.4 and 4.9 years, respectively.

### **3.5 Analysis of Property Finances**

Before we begin a discussion of the financial health of the Vermont nonprofits and their projects, it is important to establish a context. This section will identify strengths as well as areas for improvement, but the reader should understand that calling for improvement does not mean that the system or its actors are drastically flawed. Real estate development is a

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<sup>20</sup> Anglin, R. and McNeely, J.; “ The Role of Employee Benefits in Building a High-Impact, High-Performance Community-Based Development Organization.”

risky venture, especially rental development, where the investment is relatively illiquid and subject to risk over a long period of time. In any sample of projects, some will struggle, and a few will probably fail. Even the most adroit developers experience failure. In comparison to a number of other states and large cities, ICF believes the Vermont system performs well.

Based on extensive research the President's Millennium Commission on Housing has published findings recommending that public programs be prepared to either establish significant reserves up front or be prepared to inject funds during the compliance periods for affordable housing projects, due to the probability of projects experiencing financial difficulty. For example, from our other housing work, we know of one large southeastern state, with skilled underwriters, and durably-built projects, that is currently suffering such extreme vacancy losses in its HOME-funded projects that it fears many of them will fail and has asked HUD for relief. Another large southwestern state HOME Program has HOME projects opening their doors this year, that appear to be in financial difficulty at the outset, due in large part to increases in utility and insurance costs since the underwriting was completed. Beyond the vagaries of the real estate business, other types of failures occur. In major cities like Washington, DC and Kansas City, MO and the State of Texas (though Texas is not alone) dozens of projects, funded with millions of dollars, are never completed or never achieve compliance with program rules due to the incompetence or venality of the developers. In these programs developers blatantly defy the rules, pocket revenue, and allow projects to decay so that value is lost before the funding entity can react. The Vermont system that provides for multiple skilled underwriters to review project financing, allows for reevaluation of funding as projects are developed, and provides monitoring and assistance to built projects appears to have avoided these major problems.

ICF's belief in Vermont's performance is supported by other objective data sources. In HUD's HOME Snapshot Performance Rating System, Vermont's HOME program, administered by VHCB, is ranked as the fourth best state (of 51, including Puerto Rico) in HOME performance. This ranking is based on a wide range of measures, from units completed to timeliness of disbursements to level of income tenant served.

To provide a picture of finances in the study projects, ICF requested data for study projects, and analyzed total operating expenses and net operating income. Note: The data below illustrate the *short-term* experience (the most recent 12-17 months) of a limited number of projects<sup>21</sup>. Due to the variability between projects and fluctuations within individual projects over time, it is not possible to generalize about the system or any particular developer based on this data. It is important, however for readers to realize that projects that fall outside expectations can dramatically affect an organization's financial health. It is also vital going forward that this data be collected for a broad range of projects and entered into a central database so that analysis can be performed to inform future underwriting.

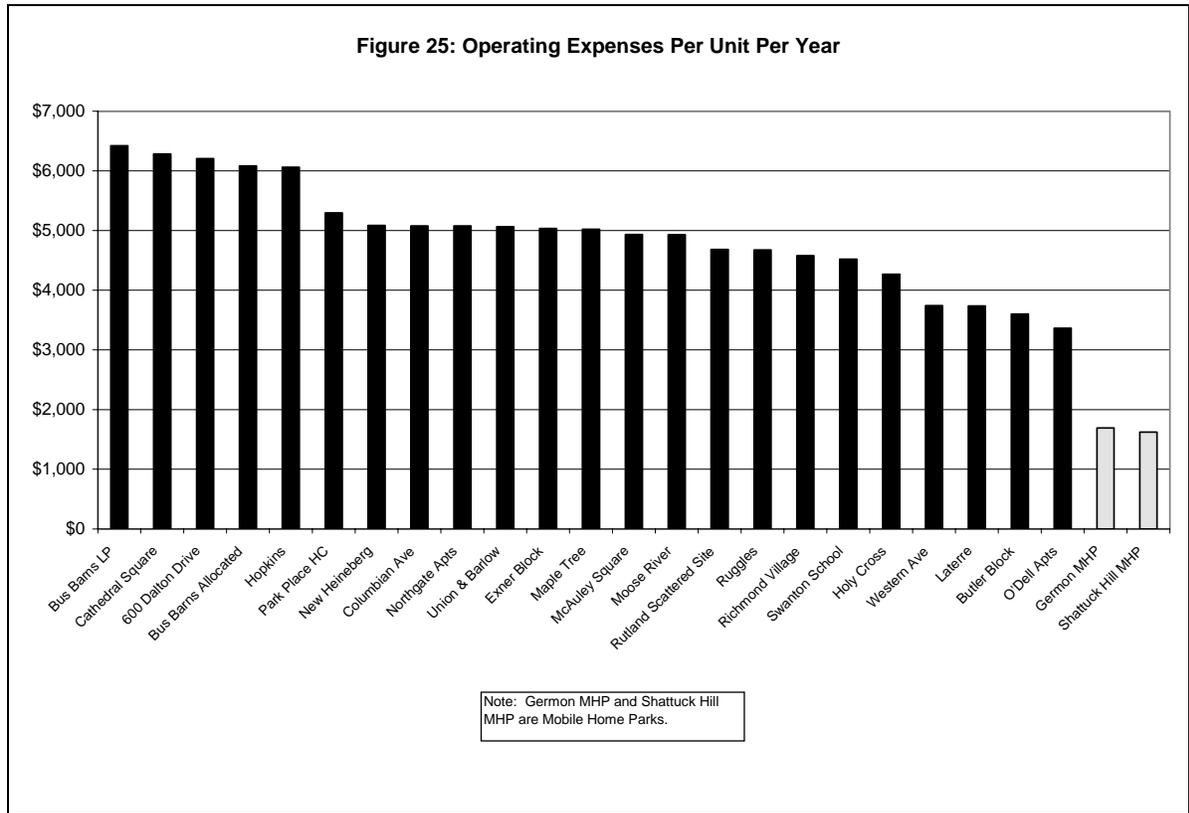
### **3.5.1 Operating Expenses**

Figure 25 below depicts the broad range of per unit operating expenses. While the average annual per unit expense level was \$4,682, individual properties showed a great

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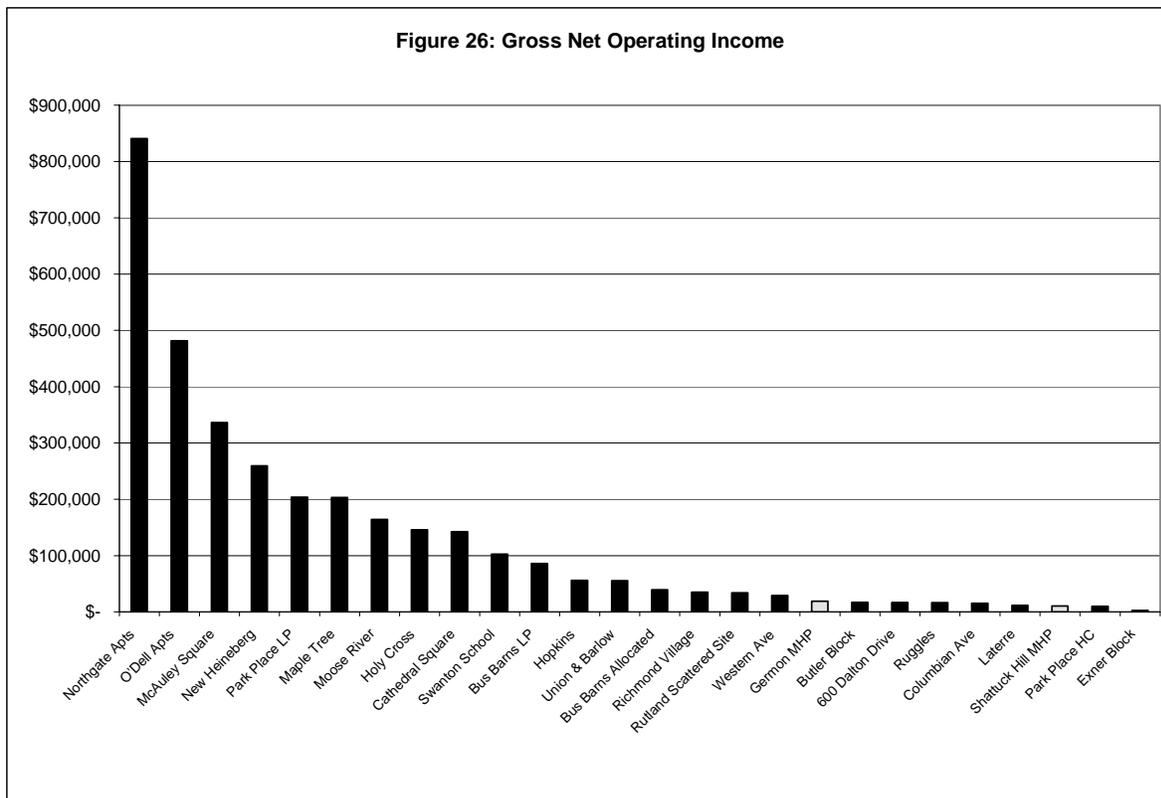
<sup>21</sup> Property operations data were available for 28 of the 36 studied projects. One organization, RAHC, did not respond to requests for property operations data. Data provided on four other properties had significant discrepancies that could not be resolved to ICF's satisfaction and were withheld from this analysis.

deal of dispersion. The projects with operating expenses well above the average tended to be those that paid utilities in excess of \$1,000 per unit. Other above norm projects were rehabilitation projects or served people with special needs, or both, and so had high administrative and maintenance costs.



### 3.5.2 Net Operating Income

Perhaps the most important single number about a property is its net operating income (NOI)-- the difference between income and operating expenses. NOI is important for many reasons. NOI is used by appraisers to help determine value, and it is the key figure used to determine the debt that a property can support or equity it can attract. Figure 26 summarizes NOI for the study projects. While all projects have positive NOI, there is a great deal of range, from projects that are operating just above break-even to a few projects, such as Northgate, that have significant NOI (\$840,822). Of the nine projects with the largest NOI, seven are in Chittenden County, where rents are higher and projects, based on their higher NOI, can be financed with greater debt. For example, after paying operating expenses, the Northgate project still has a \$580,000 debt service payment to make and a \$85,000 deposit for replacement reserves, payments which are drawn from NOI. The other two projects with the highest NOI were financed through the U.S. Department of Agriculture Rural Housing Service's (RHS) Section 515 program, meaning that they have one percent mortgage financing and rental assistance contracts (paid by RHS) which are sized to help cover this debt service.



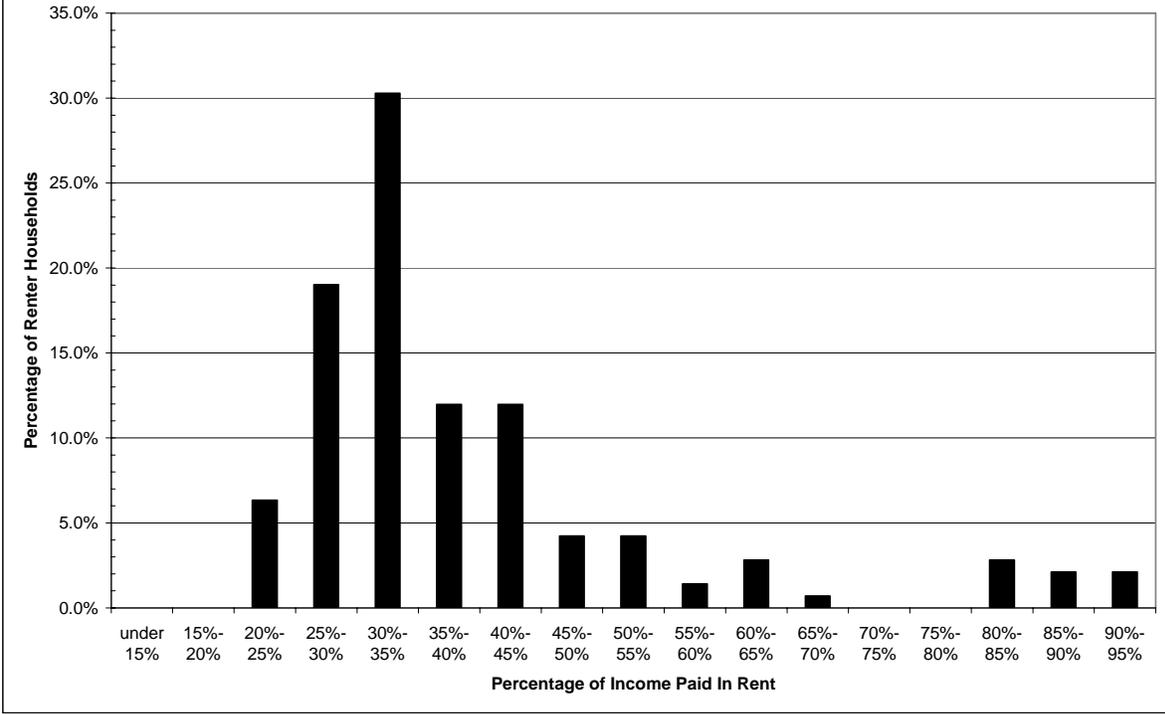
Limitations on Rental Revenue

When we examine income, several related questions arise: Could rents be higher? Are tenants benefiting inordinately from the subsidies that the State provides? Vermont's housing nonprofits are limited in the amount of rent they can charge for two reasons: one, funding source requirements limit rents to certain levels and mandate that they serve low- and very-low income households; and, two, the limitations on the ability of the tenants served to pay rent as a result of their limited incomes.

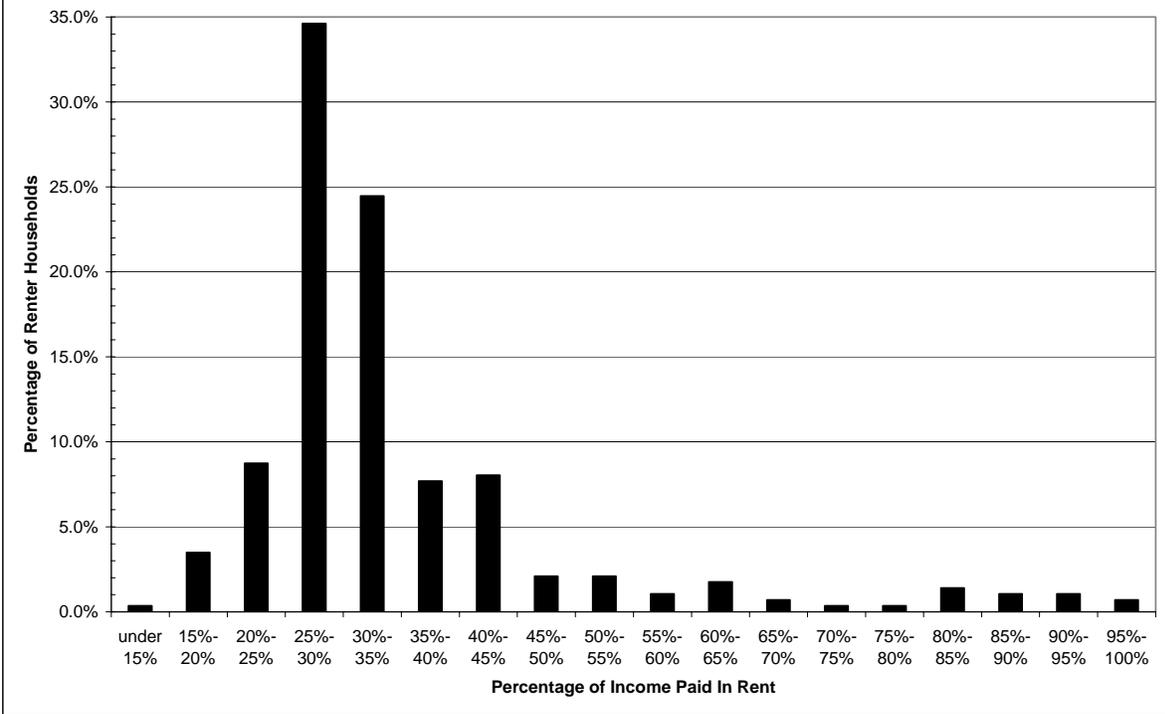
The common standard for "affordability" is payment of approximately 30% of gross income for housing rent and utilities. This standard is used by HUD for setting rents and assistance levels in a number of programs. We evaluated the "rent burden", or percentage of income paid for gross rent (including utilities) from rent rolls provided VHCB for a sample of 14 projects.<sup>22</sup> Figures 27 and 28 summarize gross rents as a percentage of income for all income-restricted units and for the subset of restricted units in which tenants *did not* receive rental payment assistance. Given that rental assistance payments are designed for tenants to pay 30% of income for rent, the most meaningful figures are those that look at rent burden only for units without rental payment assistance (Figure 27). No tenants in income-restricted units without rental assistance units pay less than 20% of income for rent, while 32% of tenants in these units pay more than 40% of income in gross rent and 16% pay more than 50% of income in gross rent. Clearly, there is little or no room for rent increases.

<sup>22</sup> Rent rolls showed the most recently available occupancy data including: household income, income as a percentage of area median income (adjusted for household size), tenant rental payment, utility payment (if tenant paid), and an indication of whether the tenant received rental payment assistance (e.g., Section 8).

**Figure 27: Rent as a Percent of Income for Non-Section 8 Restricted Units**



**Figure 28: Rent as a Percentage of Income for All Rent Restricted Units**



Readers are reminded that while this analysis shows a substantial share of rent burdened households, this analysis does not account for household circumstances prior to renting a VHCBA assisted unit (i.e., rent burdens may have been more extreme prior to leasing an assisted unit). Readers are also reminded that those on a very low income (e.g., SSI disability) have barely enough money to live on, regardless of the percentage of income paid for rent.

### 3.6 Reserves for Replacement

An important component of long-term property sustainability is assuring that sufficient reserves are on hand for the repair and replacement of major capital items, e.g. roofs, plumbing, concrete, and exterior doors and windows. Maintaining these reserves is a challenge for property owners, as contributions to reserves are typically the last payment made after all other operating expenses have been paid and the first to be skipped if there is a shortfall in net operating income. The formal process by which the appropriate level of replacement reserves is established is called a Capital Needs Assessment (CNA). Two key questions pertain to CNAs and the setting of reserve targets: “Is the CNA prepared using realistic assumptions?” and “Are targets updated periodically as conditions might change at the property?”

For this study ICF analyzed replacement reserves by determining the average monthly contribution based on reported operating results and then projecting the contributions forward to determine the total contribution over 20 years (combined with the existing balance in the account). Figure 29 indicates the number of units, the actual contributions per unit per annum (pupa), the higher of recommendations from the lender financing the project or the CNA, the current balance of reserves, and the projections of actual and recommended contributions over 20 years, combined with the current balance. No accrual of interest on deposits was calculated on these figures, as we don’t know when during the 20 years funds might be drawn against. Results were reported for 29 projects.<sup>23</sup> Only two of the 29 projects reporting data, Park Place and Daniels Block, did not have a CNA. However, BCLT, the developer of Park Place, reported that they conduct ongoing, periodic analysis of capital needs. All of the CNAs were prepared by a variety of professional firms, except one developer which does their own in-house. The CNAs typically cover 15 to 20 years of projected need, though developers reported depending more on three- to five-year projections of capital needs for budgeting and planning purposes. About half of the groups reported that updates were done periodically, typically in-house.

This analysis provides rough indicators of need, but may not provide a complete picture of the situation for each property for several reasons. First, the contributions analyzed are from a short time period (6-18 months). Second, the actual reserve needs of properties vary greatly. On-Site Insight, a premier national firm specializing in capital needs studies, found in a sample of 102 properties that the range of needs over 20 years was very wide, with 75% of properties distributed fairly evenly between \$8,000 and \$14,999<sup>24</sup> with a

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<sup>23</sup> Two mobile home parks, a lease-purchase project, and five projects not reporting results were eliminated from the chart below. RAHC, experiencing staff transitions, did not report CNA data. BCLT did not report on the Westgate project. BCLT provided separate data on the two Bus Barns projects.

<sup>24</sup> The website reference for the On-site Insight report is <http://www.on-site-insight.com/hudemo.htm>.

median need of \$12,000 per unit. This would translate to an annual contribution of \$600 per unit, assuming no escalation and no starting balance. Another professional colleague of ICF's with a consulting practice that specializes in asset management has stated he believes the appropriate annual contribution for affordable housing averages \$720 per unit per annum, resulting in a 20 year projection of \$14,400. It is important to note that these experts work with a range of properties that probably do not meet the construction and maintenance standards exhibited by the Vermont study projects. At the other end of the spectrum are a number of state Qualified Allocation Plans (the formal policy document in which each state sets standards for underwriting tax credit projects) that require annual contributions as little as \$225 - \$450 per unit, projecting at \$4,500-\$9,000 over 20 years.

As can be seen from Figure 29, the range of contributions and projected amounts is very wide. The projects for concern are those that do not reach the minimum levels required by their lenders, the project CNA, or the minimums mentioned above. Please note that the important numbers for consideration in the chart are the actual contributions and the projected actual amounts over 20 years. The projected CNA/lender amounts may be very low if a low, or no, recommendation was made. The CNA/lender projections are provided primarily to highlight the differences in policy and process, and the shortfalls that may occur if projects merely follow the CNA or lender guidance. Of the 29 analyzed projects:

- Four fail to meet the minimum QAP standard for projected 20 year amounts of \$4,500 per unit.
- Thirteen meet or exceed the amount recommended by the lender, VHFA, or a formal CNA.
- Eighteen meet or exceed the minimum of the primary range (\$8,000) of needs in the On-Site Insight study.

To put these results in some perspective, the On-site Insight study of 102 projects found that 70% of their study sample faced unmet capital needs.

**Figure 29: Comparison of Recommended Deposit Levels vs. Actual Deposit Levels**

		Completion	Years rent restricted remaining	# units	Balance per unit Aug. 04	Lender recommended deposit (pupa)	CNA recommended deposit (pupa)	Projected balance at 20 years (greater of lender/ CNA)	Actual level of deposit (pupa)	Projected balance at 20 years (based on actual levels)
GHT	Daniels Block	1/1/04	N/A	25	\$146	\$350		\$7,146		\$146
	Moose River	1/1/02	14	28	\$1,696	\$1,403		\$29,756	\$1,210	\$25,896
BACLT	Western Avenue	12/28/02	13	13	\$963	\$462	\$310	\$10,203	\$462	\$10,203
	Laterre House LP	12/31/98	0	7	\$175	\$300	\$432	\$8,815	\$88	\$1,935
BCLT	Maple Tree Place	8/10/02	28	50	\$862	\$432	\$864	\$18,142	\$447	\$9,802
	600 Dalton Drive	10/28/97	8	11	\$2,630	\$288	\$756	\$17,750	\$288	\$8,390

		Completion	Years rent restricted remaining	# units	Balance per unit Aug. 04	Lender recommended deposit (pupa)	CNA recommended deposit (pupa)	Projected balance at 20 years (greater of lender/ CNA)	Actual level of deposit (pupa)	Projected balance at 20 years (based on actual levels)
	<b>Park Place</b>	3/1/99	25	34		\$252		\$5,040	\$185	\$3,700
	<b>Bus Barns Allocated</b>	10/23/01	12	12	\$1,102	\$300	\$924	\$19,582	\$505	\$11,202
	<b>Bus Barns Bond</b>	12/20/02	12	13	\$1,262	\$300	\$744	\$16,142	\$782	\$16,902
<b>LHP</b>	<b>Jeffersonville</b>	11/28/01	28	32	\$949	\$370	\$452	\$9,989	\$392	\$8,789
	<b>Portland &amp; Main</b>	6/14/00	26	8	\$4,150	\$1,061	\$600	\$25,370	\$1,061	\$25,370
	<b>Brewster River</b>	12/30/97	4	7	\$1,489	\$223		\$5,949	\$223	\$5,949
	<b>Copley House</b>	9/1/01	30	22	\$591	\$368		\$7,951	\$368	\$7,951
<b>LCHDC</b>	<b>Swanton</b>	2/24/00	26	16	\$3,364	\$972	\$474	\$22,804	\$711	\$17,584
	<b>Richmond</b>	3/20/98	9	16	\$1,792	\$300	\$233	\$7,792	\$300	\$7,792
	<b>Butler</b>	4/10/03	14	6	\$354	\$600	\$600	\$12,354	\$640	\$13,154
	<b>O'Dell</b>	2/28/03	39	160	\$495	\$366	\$360	\$7,815	\$368	\$7,855
<b>RCCLT</b>	<b>Rutland</b>	9/1/93	12	31	\$2,349			\$2,349	\$615	\$14,649
	<b>Columbian</b>	2/1/02	13	9	\$1,188			\$11,188	\$500	\$11,188
	<b>Hopkins</b>	2/1/00	46	12	\$4,527	\$1,218		\$28,887	\$1,218	\$28,887
	<b>Union &amp; Barlow</b>	9/1/00	46	12	\$4,092	\$1,113		\$26,352	\$1,113	\$26,352
<b>CSC</b>	<b>Heineberg</b>	11/22/89	16	82	\$2,587	\$160	\$198	\$6,547	\$304	\$8,667
	<b>Ruggles</b>	8/26/02	23	15	\$974	\$300		\$6,974	\$395	\$8,874
	<b>McAuley Square</b>	1/25/02	23	74	\$785	\$291	\$336	\$7,505	\$297	\$6,725
	<b>Cathedral Square</b>	7/11/03	35	108	\$2,712		\$249	\$7,692	\$268	\$8,072
<b>HV</b>	<b>Howard Block</b>	9/1/03	14	13	\$260	\$290	\$461	\$9,480	\$152	\$3,300
	<b>Holy Cross</b>	1997	8	40	\$1,719	\$293	\$350	\$8,719	\$298	\$7,679
	<b>Exner Block</b>	1999	10	13	\$1,387	\$494	\$385	\$11,267	\$502	\$11,427
	<b>Northgate</b>	1/1/89		336	\$1,794	\$318		\$8,154	\$253	\$6,854

Four important recommendations stem from this section:

1. The current minimum reserve contribution required by VHFA of \$300 per unit per year is probably inadequate to meet needs unless a reserve account is funded up front. Given the difficulty of generating ongoing operating income, ICF recommends substantial initial capitalization of reserves.
2. CNAs must be done and periodically updated and a strategy developed for meeting financial needs, whether through contributions to reserves or new financing.
3. CNAs prepared by an outside firm should be cross-evaluated by the person responsible for managing the property's day-to-day maintenance, for thoroughness and accuracy of the assumptions used.
4. Staff for each developer should continue to expand in-house expertise that enables them to update their CNAs on a regular basis. Ideally the formal CNA is completed every 5 years, and every year a plan for upcoming repairs and evaluation of reserve levels is completed. Capital needs assessment is a complex task utilizing construction, engineering and economic forecasting skills. Even the most experienced and knowledgeable practitioners are not perfect at it.

## **4.0 Housing Delivery System**

The affordable housing delivery system in Vermont consists primarily of three State agencies, a statewide tax credit syndicator and developer, regional nonprofit developers, and multiple local governments. There are three separate funders: VHFA for pre-development funding, bond financing and tax credits; VHCB for State and HOME funded housing loans/grants and \$10,000 "feasibility" loans; and DHCA, which provides CDBG funding. In addition to its role as a project funder, VCHB, through its operating support grants and ongoing organizational monitoring, also plays an important role in building and maintaining the capacity of the individual nonprofits.

Two questions raised in the course of the review are: "Do we need all these agencies and nonprofits to do this job?", and the related question, "Isn't the State paying an unnecessary amount of operating and overhead costs to support these entities?". This section provides ICF's assessment of these two issues.

### **4.1 Public Agencies**

In ICF's opinion, the answer to the question about coordination between the various entities is that this approach may not work in every state, but generally it works in Vermont. Each agency is smaller than it would be if all the functions were together, making them more accessible than one large entity. In this State government everyone knows everyone else, and the senior (and junior) staff seem to coordinate exceptionally well across Departments.

In regard to administrative cost, when we look at other states where the functions of the various Vermont agencies are combined, these functions are still in different divisions, still have all of their own operating infrastructure of management and support staff, still have disagreements about appropriate policy, and often are unable to coordinate work schedules so that funding cycles are uniform.

Further, each entity, with its own distinct function, mission and expertise, still needs its own professional staff. In agencies at the federal and state level, no one person has sufficient expertise to manage the variety of federal funding sources or regulatory actions that are required – CDBG, HOME, Tax Credits, Historic Preservation, Economic Development, and so on. The variety of mission and expertise in the Vermont system today produces healthy results.

Some tasks might seem duplicative, like underwriting. However, this is a task where duplication has value (i.e., a second “set of eyes” on a project often provides a useful perspective). ICF is currently working with an umbrella state housing agency where one division underwrites all projects. Unfortunately, that underwriting section has limited funds to some projects such that the state now faces work outs and may have to repay HUD millions of dollars for projects that are not being maintained as eligible affordable housing.

While this report focuses on the productivity and efficiency of nonprofit housing developers funded by the VHCB, the Board’s role in developing an effective statewide delivery system is worthy of discussion. VHCB is actively engaged in providing training and technical assistance to the nonprofit developers. This is not to say that the developers are not skilled, it is merely to acknowledge that, in this field, constant learning is required in order to thrive. VHCB also performs on-site organizational monitoring of each nonprofit at least once every two years. During monitoring, VHCB reviews financial statements and analyzes the performance of both individual projects and the nonprofit organization. We recommend that Vermont continue these practices. In ICF’s view, VHCB’S flexible, mentoring style and a strong monitoring and technical assistance program has in helped to build the capacity of the statewide nonprofit network.

One other aspect of the State’s system is noteworthy-- the partnership between VHCB and VHFA to use the 4% tax credit with bond financing. We have come across very few states that are as aggressive as Vermont in using 4% non-allocated credits with in-cap State Bonds used as construction financing. This resource is even used for projects with permanent financing from USDA’s RHS, as is the case with RCCLT. There is obviously extra work involved in combining funding sources in this way and some projects had to be split into two parts to accommodate this use. However, the overall result is a maximization of low income housing tax credit allocations and more equity available overall for housing projects in the State.

The decentralized nature of the State’s housing finance agencies could have its disadvantages (potential for lack of coordination, inconsistent priorities, applications, and application deadlines), and ICF recommends that the agencies, though their common boards, address those issues. For example, one issue that arose during the study is how DHCA, which administers the CDBG program, fits in with the funding and application cycles for the other agencies. Applicants stated that they typically had to go through two funding rounds before getting their application approved, which would add to the difficulty of moving projects along expeditiously. ICF did not investigate this issue, but we do recommend that it be considered.

## **4.2 Housing Vermont**

Another major part of the delivery system is Housing Vermont, a nonprofit established by the State to support affordable housing development. Housing Vermont carries out development, but, more importantly, provides invaluable services to the community-based nonprofit development corporations that bring projects to them. This type of entity is unique

to Vermont and is responsible in large part for the low level of failed projects in Vermont. These services include the following:

- ❑ **Pre-development:** Assistance doing feasibility analysis, packaging and securing financing, overseeing the process of developing a construction scope of work, and assembling a development team
- ❑ **Assembling tax credit equity:** Housing Vermont is particularly adept in this area. When it is possible to bring in a local lender as a tax credit investor, that is what they do. Since it has become more difficult to identify local lenders – due to bank consolidation in Vermont and throughout the country – Housing Vermont can typically place the equity in one of their equity funds that attract capital from inside and outside the State.
- ❑ **Interim financing:** Providing some or all of the construction financing for the project, either out of their own line of credit or cash assets, or through private loans secured, in part, with implicit or explicit guarantees.
- ❑ **Construction management:** This is one of the riskiest phases of a real estate development project (cost overruns and delays). Housing Vermont typically manages this phase of the development process, including managing the process of drawing down and accounting for construction financing.
- ❑ **Taking an ownership interest in the project:** Housing Vermont typically takes on the role of co-general partner. Among other things, that means that they can lend their financial strength to an otherwise risky project.
- ❑ **Asset management:** Housing Vermont has an impressive system for monitoring projects using a quantifiable quarterly review process – physically and financially – and for putting projects on a Watch List that need further attention and follow up.

Projects are generally identified by local partners, who request Housing Vermont's involvement. Generally, the partners are either local nonprofits that are new to development or do not have adequate staff to undertake these activities on their own, or experienced nonprofits engaging in a complicated project who feel they need Housing Vermont's financial strength or expertise. In exchange for the above services, Housing Vermont splits the developer fee, and sometimes earns an additional construction management and asset management fee.

The system does have some inherent tensions. As local nonprofits work on affordable housing projects with Housing Vermont, the capacity of the local nonprofit to undertake affordable housing development on their own increases. So, at least in theory, the more Housing Vermont works with a local partner, the more they will want to do development on their own, without Housing Vermont participation. Housing Vermont and local nonprofit staffs are very well aware of this dynamic. Some nonprofits only do LIHTC deals with Housing Vermont, while others only use Housing Vermont competitors (described below) and still others use Housing Vermont on some of their projects and do others on their own or with Housing Vermont competitors. The reality is that, at least up until now, there have been more than enough tax credit and other financing resources to keep Housing Vermont and the local partners busy.

Housing Vermont does have competitors. For instance, there are several in-State independent consultants who help arrange financing (one has particular expertise in USDA RHS financing), and place tax credit equity, much like Housing Vermont. However, they primarily serve as consultants on affordable housing projects, and do not take an ownership interest in projects, which Housing Vermont typically does. That means the nonprofit can run the project with less interference from a co-general partner. But it also means that the project will have to live without the financial depth that a co-owner like Housing Vermont can provide.

One of Housing Vermont's primary jobs has been to assemble equity for tax credit projects, and they have done that very efficiently. They have been able to get investors to contribute an average of \$0.89 for each low-income housing tax credit dollar awarded to their projects. We estimate, based on our experience nationally, that the market average during this period was approximately \$0.78; meaning Housing Vermont generated approximately 19% more than the market average. Since 1998, if they had sold credits at \$0.78, they would have generated \$4.7 million less than the \$28.7 in equity that they did generate.

### 4.3 Local Nonprofit Developers

One unique aspect of the Vermont system that was immediately apparent to the ICF team is that there are nonprofit providers that cover each of the regional housing markets in the State, a conclusion that was seconded by Liz Nickerson of the Federal Home Loan Bank of Boston in her memo to the ICF research team. Few states, especially rural states, can boast comprehensive coverage for small rural communities. Of course this apparent quality invites another reasonable question--whether the system benefits by providing funds to so many local, community-based nonprofit developers, or whether some consolidation should be encouraged. We have discussed earlier the broad range of mission accomplished by these developers. Advantages they bring to the development process itself through their ongoing presence and participation in local community life include:

- ❑ **Project identification:** It is easier for these entities to be opportunistic; i.e., to identify projects that are critically needed in the community and focus on those most beneficial, because of their knowledge of community needs and neighborhood dynamics. In many cases they are approached by local owners or local government, because they are known as reliable community-oriented entities with sophisticated development skills and resources.
- ❑ **Project selection and marketing:** Knowledge of and ongoing activity in the local low-income rental market enables the nonprofits to both understand and access the market of potential renters or buyers much more easily than other developers.
- ❑ **Permitting:** While many of their projects do face permitting delays, they are able to overcome some opposition that a private developer might not.
- ❑ **Local government collaboration:** They have direct, regular access to the departments of local government that can assist them or to whom they have regulatory obligations.
- ❑ **Public involvement and fundraising:** They are able to enlist public support, often in the form of hard dollars to support projects and their own operation.

- ❑ **Stewardship:** These organizations are the stewards of the properties in perpetuity. Their local credibility and ability to operate effectively will depend on their ability to manage their properties well.
- ❑ **Limited scope of risk:** The fact that there are multiple organizations operating limits the impact of an organizational failure on the system as a whole.
- ❑ **Community accountability:** The organizations are governed by citizens representing a broad spectrum of the communities in which they operate.

There are some disadvantages in having multiple developers around the State. These include:

- ❑ **Difficulty in maintaining organizational capacity:** There are a limited number of highly skilled professionals in any one community. A local nonprofit may encounter periodic difficulty in recruiting professionals, which may be a significant issue given the tenure figures previously reported.
- ❑ **Limited financial resources:** Smaller portfolios and limited size of management operations may cause some inefficiencies and creates less cushion when one project is in trouble financially.
- ❑ **Additional workload for funding agencies:** State agencies must work with a range of organizations with different skill levels and personalities.

#### 4.4 Ongoing Measurement of Financial Data

State decision makers expressed a desire to monitor the financial health of the system on an ongoing basis and asked ICF to consider this issue in our report. This section provides ICF's observations on how to achieve this goal. The first data source of choice, because it is certified by a qualified third party, is the audited financial statement of the developer. While this is a place to start, the typical audit will not be particularly useful in giving a true picture of real estate development operations. The audit is useful for identifying the existence or lack of adequate controls; determining the accuracy of the organization's accounting; and establishing a big picture view of inflows, outflows, assets and liabilities. As explained below, it does not enable one to determine the ongoing efficiency or effectiveness of development activities, the availability of cash for operations or reserves, future risks, or the true value of assets:

- ❑ **Efficiency and effectiveness:** The financial statement of revenue includes both capital grants and revenue from operations, in addition to other items. Expenses include depreciation, which is only a proxy for the real devaluation of an asset. Both include activities where the organization acted as a fiduciary, and operations are not affected. To get a real picture of revenues versus expenses, someone familiar with the organization would need to analyze finances from a different perspective and level of detail than that required in the annual audit. Such detail would exclude capital grants, depreciation and fiduciary actions in order to achieve a better analysis of operating soundness.
- ❑ **Identification of future risks:** The audited statements may show increases to reserves as required, but would not reflect, for example, whether those reserves were actually the right amount to meet the future needs of the property. Real estate

development is a risky, cyclical business. Only a crystal ball could predict whether revenue streams from development fees or cash flow from projects will continue. Strategic planning within the organization is needed to deal with that problem.

- ❑ **Availability of cash for operations and reserves:** The audited financial statement does not distinguish between cash that is needed for the daily operation of properties, and is de facto restricted in that sense, and cash that is available for optional activities. While organizations may have large amounts of cash on hand at any given time, none report significant operating reserves for the organization, and our analysis of financial statements supported that finding.
- ❑ **Valuation of assets and change in net assets:** Revenue in the form of capital grants is typically converted to assets as it is loaned to or invested in projects. This is the primary component of change in net assets and is only a measure of the level of capital funding that organization received that year, not really a measure of performance. These assets are then valued at cost minus accumulated depreciation. This valuation method has almost no relationship to the true value of the asset, which, in the rental business, is determined primarily by the asset's ability to generate future revenue. This would have to be determined by detailed, periodic appraisals of properties, but even this approach is somewhat meaningless, as the asset is committed to its current use in perpetuity. The asset's primary value is its provision of affordable housing to the community. When properties do change hands, detailed appraisals are done and new financing is based on that analysis. Tax credit partnership valuations are treated differently by different auditors, but the same issues pertain.

Given the above, ICF makes the following recommendations:

1. Have organizations continue to report financial results project by project to the funding Agency. Interested State decision makers should review these reports. Disaggregated costs for maintenance and other items are available there. To see an overall picture, someone in the system might aggregate projects into a master spreadsheet for each developer.
2. Have organizations report revenue and expenses excluding capital grants, depreciation, and fiduciary activities.
3. Continue to provide coordinated planning, market study, and training activities.

## 5.0 Summary of Major Findings and Recommendations

ICF's evaluation shows that the nonprofit provider system is meeting its statutory goals and providing affordable housing in an effective manner within the statutory and Consolidated Plan constructs. Development of affordable housing is by nature a high-risk, low-return undertaking. In ICF's opinion, the Vermont system has the technical capacity and funding mechanisms necessary to effectively manage these challenges. This section briefly summarizes ICF's major findings and makes a targeted set of related recommendations.

### 5.1 PROJECT DEVELOPMENT PRACTICES

#### Findings

1. **Professionalism of Development Practices:** Studied nonprofits exhibit a high level of professionalism with respect to project development practices. From their use of third party cost estimates to their ability to acquire sites at discounted costs, the organizations are models for other nonprofits to emulate.
2. **Compliance with Consolidated Plan Priorities:** Studied projects comply with Consolidated Plan and statutory priorities.
3. **Development Costs:** Development costs have been escalating in recent years. However, considering the factors affecting development and the costs of the projects studied in comparison to other cost benchmarks, ICF concludes that the cost for studied projects is within, or, in some cases, below expectations.

#### Recommendations

1. **Cooperative Purchase:** Establish a cooperative purchasing program for professional and periodic services. Insurance, fire extinguisher monitoring and maintenance and elevator service are all examples of services benefiting from central purchasing.
2. **Market Studies:** In light of the fact that only 20 of 36 studied projects had market studies performed, VHCB should consider requiring studies as a condition of funding on all projects as VHFA has.
3. **ConPlan Priorities:** As noted during the discussion of project costs, some of these priorities do have development cost implications, but also provide significant housing and non-housing community and economic development benefits. The appropriate forum for debating the cost-benefit of the tradeoffs between these priorities is through the Consolidated Planning process.
4. **Development Fees:** The nonprofit housing system is dependent on development fees. Development fees in many cases are being used to subsidize property management and social service delivery components that are not self-financing due to mission-driven, regulatory limits on rental revenue. It is important that nonprofits maintain and maximize their development fees. Given VHFA's tax credit guidelines (and those standards set by other states), higher fees are permissible within the current framework. It is generally true that if nonprofits were to raise their development fees they would

typically be funded by additional subsidy; however, ICF believes that it is important for the nonprofits' costs to be covered. To provide the right level of funding in making funding decisions, State decision makers should balance the provision of development fees and operating support grants based on some knowledge of the financial position and operations of the organization. In addition, it is critical that sufficient capital support be provided to each project to allow for positive ongoing operating revenue and contributions to capital reserves. All of these factors are related in their impact on the long-term durability of the housing and its management.

5. **Continue to Evaluate Costs:** It is essential that Vermont decision makers have access to good data about housing development costs. ICF strongly recommends that there be open and widespread sharing of detailed cost data for all private and nonprofit sector projects, including comparable information about features, quality, location, and public benefit. VHCB should continue to conduct analyses such as the Cost Memo and evaluate development costs in the proper context of current market conditions and the multiple Consolidated Plan goals that projects achieve. In analyzing and comparing costs, it is essential that the long-term costs and benefits of preserving affordable housing versus allowing it to transition into non-income-restricted property be calculated and considered. In general, permanent affordability avoids the costs of displacement and relocation of in-place low-income tenants, transfer costs, and the high cost of replacement housing.

## 5.2 NONPROFIT AND PROPERTY MANAGEMENT

### Findings

1. **Management Systems:** Appropriate organizational management systems are, for the most part, in place.
2. **Indicators of Financial Health:** Financial health of studied nonprofits is within expectations for organizations in the affordable housing business.
3. **Operating Grants:** Operating grants constitute a relatively small share of organizational budgets and provide significant benefits to the housing system.
4. **Salaries:** Salaries are within expectations for nonprofit organizations but low in comparison to similar categories of jobs within Vermont. Tenure is low compared to national averages.
5. **Property Operations:** Analysis of NOI shows that all projects are operating at or above break-even. Additional analysis beyond the scope of this project should be conducted to examine the relationship between underwriting assumptions, intervening project circumstances (e.g., increases in insurance costs, property taxes, etc.) and long-term project operations.
6. **Rent Levels:** Analysis of rent rolls shows that a significant share of units are leased to very-low and low- income households, that rent burdens are within expectations, and that rents cannot be increased without displacing current tenants.

7. **Replacement Reserves:** The current minimum reserve contribution required by VHFA of \$300 per unit per annum is probably inadequate to meet needs unless a significant reserve account is funded up front.

### Recommendations

1. **Create Asset Management Plans:** Only three studied organizations had a formal asset management plan. As the Vermont nonprofit system matures, the potential for supporting the sponsoring nonprofit organization from management and maintenance fees becomes feasible. Each portfolio needs professional asset management plans that look at the refinancing, rent rolls, and resyndication opportunities at the 15 to 30 year point.
2. **Hedge Oil Costs:** In Vermont, most affordable rental properties pay for heat (as opposed to tenants). The owner of the property is absorbing the long-term risks of oil price increases. Oil is a highly volatile commodity that can be affected adversely by politics and world affairs. Currently, heating costs are usually the largest single expense item after property tax. This contingent liability should be addressed with hedging techniques. Consider the creation of an oil purchasing co-op.
3. **Negotiate Group Insurance:** Property insurance costs have escalated between 15% and 19% in 2003 as the insurance industry moved from a soft market into a hard market. Without group coverage it may become difficult to even maintain insurance, much less get affordable and economic coverage in the future.
4. **Continue Operating Grants:** Operating grants play important roles in the nonprofit system: enhancing the delivery of resident services, supporting targeted capacity building activities and purchases (e.g., upgrading of accounting software), and sustaining organizations when they aren't garnering sufficient development fees to subsidize property management and resident service functions. Long-term affordability requirements restrict the revenue potential of properties, so nonprofit owners and managers may from time to time struggle to break even from ongoing operating revenue alone. With the private sector, we provide tax benefits and other incentives to assure the pursuit of ventures serving public interest goals that otherwise might not be economically attractive. Operating grants to nonprofits serve the same function.
5. **CNA Protocols:** CNAs must be performed and periodically updated along with a strategy for meeting the financial needs, whether through contributions to reserves or new financing. CNAs prepared by outside firms should be cross-evaluated by a second person for thoroughness and accuracy of the assumptions used. Ideally a formal CNA will be completed every five years, and a plan for upcoming repairs and evaluation of reserve levels will be completed every year.
6. **Sponsor CNA Training:** Capital needs assessment is a complex task utilizing construction, engineering and economic forecasting skills. Even the most experienced and knowledgeable practitioners are not perfect at it. Staff for each developer should continue to expand in-house expertise that enables them to periodically update their CNAs.

## 5.3 DELIVERY SYSTEM

### Findings

1. **Multi-Layered, Effective System:** The multi-layered housing delivery system provides the State with a range of highly specialized expertise. Although this expertise is housed in a number of different organizations, the system is well coordinated. While the segmented delivery system might not prove effective in every state, it appears to be working well in Vermont. This is largely due to the sophistication of the funding entities and the level of coordination that takes place among them.

### Recommendations

1. **Continue Flexible Style:** Maintain VHCB's operating style and delivery system. Their collaborative mentoring approach and flexible underwriting augmented with training and careful organizational monitoring has strengthened and hardened the nonprofit industry in Vermont appropriately.
2. **Tax Credit Scoring:** For tax credit scoring in the future, add two points for projects that preserve permanent affordability. This will become extremely important in the future as previously developed projects return to the syndication pool.
3. **Expand Asset Management Role:** Create an asset management and/or project refinance specialist on staff. Going forward, VHCB will see a steady flow of projects financed in the 1980s that require buyout of the tax credit partners and, possibly, renovations. It will be informative to monitor the capital needs and refinancing strategies for properties as ownership is transferred, in order to develop cost effective strategies. Should VHCB wish to project overall capital needs for the existing stock of housing, that projection would include the following components:
  - A timeline for when the tax credit partners must be bought out, along with the projected cost of the buyouts;
  - Analysis of capital needs for repairs and modernization;
  - Analysis of cash flow and debt capacity; and
  - Analysis of potential for new tax credit syndications.
4. **Reporting:** The system can be improved through better data reporting systems. A great deal of valuable information is already being reported but not in a uniform format or in electronic files, which would aid analysis by VHCB and other policy-makers. For example, operating statements for properties are provided in paper copy and in a wide-variety of reporting formats. Similarly, VHCB reviews organizational financial statements during monitoring visits, but this information is not collected in a central database so that trends, both at the organization and system level, can be tracked over time.